SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938

No. 18

JAMES E. DAVIDSON, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

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[fol. a] [Caption omitted]

[fol. 1] **BEFORE UNITED STATES BOARD OF TAX APPEALS**

Docket No. 72904

JAMES E. DAVIDSON, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

DOCKET ENTRIES

Appearances:

For Taxpayer: Geo. Rogers, Esq., John E. Walker, Esq., E. J. Svoboda, Esq., J. A. C. Kennedy, Esq., Claude M. Houchins, Esq.

For Comm'r: E. C. Algire, Esq.

1933.

July 10. Petition received and filed. Taxpayer notified. (Fee paid.)

July 10. Copy of petition served on General Counsel.

Aug. 2. Answer filed by General Counsel.

Aug. 14. Copy of answer served on taxpayer.

Oct. 21. Motion to consol. with Docket 61741 and 72405 for Circuit hearing at Omaha filed by General Counsel. 10/25/33 Granted and consolidated.

1935

May 2. Hearings set at Omaha, Nebr. week of June 3, 1935.

June 11. Hearing had before Mr. C. P. Smith, Div. 5, Submitted on merits. Appearance of Mr. Svoboda filed. Briefs due, pet's 7/25/35, respondent's 8/9/35, pet's reply 8/24/35.

June 19. Stipulation of facts filed.

June 19. Stipulation re photostatic copies initialed E. J. S. and E. C. A." filed.

July 1. Transcript of hearing of June 11, 1935, filed.

July 24. Motion for extension to Aug. 5, 1935, to file brief filed by taxpayer. 7/24/35 granted. Pet's brief due Aug. 5, 1935. Respondent's brief due Aug. 20, 1935, Pet's reply brief Sept. 4, 1935.

[fol. 2]

July 26. Motion for leave to file amended answer, amended answer lodged, filed by General Counsel. 8/5/35, Granted.

Aug. 5. Memorandum brief filed by taxpayer. 8/5/35 copy served.

Aug. 20. Brief filed by General Counsel.

1936.

May 8. Findings of fact and opinion rendered, Mr. Smith, Div. 5. Judgment will be entered under Rule 50.

May 23. Motion to correct the findings of fact filed by General Counsel.

June 12. Notice of settlement filed by General Counsel.

June 15. Order that motion filed 5/23/36; and the findings of fact contained in the Board's report promulgated 5/8/36 be amended, entered.

June 16. Hearing set July 8, 1936 on settlement.

July 8. Hearing had before Mr. Turner on settlement. Not contested—Referred to Mr. Smith for decision.

July 10. Decision entered, Eugene Black, Div. 15.

Oct. 10. Notice of appearance of Claude M. Houchins as counsel, filed.

Oct. 10. Motion to vacate decision and for rehearing and reconsideration filed by taxpayer. 10/12/36 denied.

1937.

Jan. 12. Notice of appearance of George Rogers as counsel filed.

Jan. 12. Petition for review by United States Circuit Court of Appeals, Eighth Circuit, with assignments of error filed by taxpayer.

Jan. 12. Proof of service filed by taxpayer.

Mar. 5. Agreed præcipe filed—with proof of service thereon.

[fol. 3] Before United States Board of Tax Appeals

[Title omitted]

Petition of James E. Davidson for Appeal—Filed July 10, 1933

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commis-

sioner of Internal Revenue in his notice of deficiency dated May 12, 1933 and as the basis of his appeal sets forth the following:

1. The petitioner is an individual whose address is 5209 Burt Street, Omaha, Nebraska.

2. The notice of deficiency (a copy of which is attached hereto, made a part hereof and marked "Exhibit A") was mailed to the petitioner May 12, 1933.

3. The tax in controversy is income tax for the calendar year 1929 in the amount of $9,352.50 asserted against the petitioner.

4. The determination of tax set forth in said notice of deficiency is based upon the following error:

(a) The action of the Commissioner in improperly computing profit upon the sale of:

1. 3200 shares National Power & Light Company Common Stock.

2. 100 shares General Electric Company Common Stock.

The above securities were sold by the petitioner during 1929 and the Commissioner erred in applying to the proceeds of said sales the cost of certain blocks of the same class of securities which, in fact, the petitioner did not sell and the Commissioner failed to consider as the cost of the securities sold the cost of the blocks thereof which, in fact, were sold.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) 1. Prior to the year 1929, the petitioner had purchased certain shares of common stock of National Power & [fol. 4] Light Company which the petitioner, from the time of the original acquisition of such shares, considered as part of his permanent investments or "estate". Prior to January 1, 1929, the petitioner had placed with his broker 900 shares of said common stock of National Power & Light Company, with the specific understanding between the petitioner and his broker that such stock was to be considered at all times as "collateral stock", not to be sold unless specifically instructed by the petitioner or as might be necessary to protect the broker.

During the taxable year involved the petitioner purchased and sold, through his broker, certain blocks of National Power & Light Company common stock. In his tax return, the petitioner computed the profit incident to such sales by applying against the sales price the cost of various blocks of the same securities previously purchased specifically for trading purposes. The Commissioner has ignored the petitioner's allocation of securities sold to the blocks of securities specifically purchased by the petitioner for resale and has substituted therefor an arbitrary allocation of the securities erroneously assuming the sale of the petitioner's collateral stock.

2. On February 19, 1929, the petitioner purchased at a cost of $22,705.00 100 shares of General Electric Company common stock along with several other security purchases at the same time and made payment to the broker for said purchase on February 20, 1929 from the proceeds of a loan made specifically for said purchase from The Omaha National Bank. At the time payment was made for the securities instructions were given to the broker that they be delivered to the bank from which the loan was secured, to be held by the bank as collateral for the loan. The bank received said securities on March 4, 1929, among which was included certificate No. N. Y. C. 86242, dated February 26, 1929, in the name of James E. Davidson, for 100 shares of General Electric Company common stock. On March 26, 1929, said 100 shares of stock were sold by the broker for $22,791.00 to cover which there was delivered to the broker by the bank certificate No. N. Y. C. 86242 which had been received by the bank on February 26, 1929, the proceeds of said sale being delivered direct to the broker from the bank to apply on the loan previously negotiated for the purchase thereof.

The Commissioner has ignored the foregoing facts and has erroneously considered as the cost of the shares sold certain other General Electric Company common stock [fol. 5] owned by the petitioner and purchased a number of years prior to the taxable year involved herein.

6. The petitioner prays for relief from the deficiency asserted by the respondent in the following particulars:

(a) 1. The petitioner claims that the computation of profit realized upon the sale of the common stock of National

Power & Light Company is correct as reported in his tax return as filed and that the Commissioner should recognize, in his identification of the lots of securities purchased, in determining the cost of the securities sold, the petitioner's clear distinction as shown by his records between the securities purchased and held by the petitioner's broker for the petitioner as collateral and other securities of the same class purchased by the petitioner for trading purposes and, as such, sold by him.

2. The petitioner claims that the computation of the profit realized upon the sale of the common stock of General Electric Company is correct as reported in his return as filed and that the Commissioner should give proper consideration to the actual facts of the transaction. These facts clearly show the cost of the specific lot of the securities purchased which is applicable to the subsequent sale thereof made within the same taxable year.

Wherefore, the petitioner prays that this Board may hear and redetermine the deficiency herein alleged.

John E. Walker, Counsel for Petitioner, 1001 15th Street, N. W., Washington, D. C.

Duly sworn to by James E. Davidson. Jurat omitted in printing.

[fol. 6] EXHIBIT "A" TO PETITION

Treasury Department, Washington

Office of Commissioner of Internal Revenue

May 12, 1933.

Mr. James E. Davidson, 5209 Burt Street, Omaha, Nebraska.

SIR:

You are advised that the determination of your tax liability for the year(s) 1929 discloses a deficiency of $9,352.50, as shown in the statement attached.

In accordance with section 272 of the Revenue Act of 1928, notice is hereby given of the deficiency mentioned. Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter, you may petition

the United States Board of Tax Appeals for a redetermination of your tax liability.

However, If You Do Not Desire To Petition, you are requested to execute the inclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this form will expedite the closing of your return(s) by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the inclosed form, or on the date assessment is made, whichever is earlier; Whereas If This Form Is Not Filed, interest will accumulate to the date of assessment of the deficiency.

Respectfully, David Burnet, Commissioner, by W. T. Sherwood, Acting Deputy Commissioner.

Inclosures: Statement. Form 870.
Copy. 6-29-33. SAE.

[fol. 7] Statement

IT:AR:D-1. LD-60D.

In re Mr. James E. Davidson, 5209 Burt Street, Omaha, Nebraska

Income Tax Liability

Year	Income tax liability	Income tax assessed	Deficiency
1929	$9,352.50	None	$9,352.50

The deficiency shown herein is based upon the report dated November 11, 1931, prepared by Revenue Agent A. D. Berliner, and transmitted to you under date of November 21, 1931, which report is made a part of this letter.

Careful consideration has been accorded your protest dated December 1, 1931, in connection with the findings of the examining officer, and the information submitted at a conference held in the office of the internal revenue agent in charge.

Inasmuch as the year 1928 is before the United States Board of Tax Appeals for the same issue, this formal notice of deficiency is being mailed.

A consen' which will expire June 30, 1934, except as extended by the provisions of Section 277 of the Revenue Act of 1928 is on file for the year 1929.

Copy. 6-29-33. SAE.

BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

ANSWER OF COMMISSIONER OF INTERNAL REVENUE—Filed August 2, 1933

Comes now the Commissioner of Internal Revenue by his attorney E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue, and for answer to the petition filed in the above-entitled proceeding admits and denies as follows:

1, 2, and 3. Admits the allegations contained in paragraphs 1, 2, and 3 of the petition.

[fol. 8] 4. Denies that the Commissioner of Internal Revenue erred in manner and form as alleged in paragraph 4 of the petition, sub-paragraph (a).

5. Denies all of the allegations of fact contained in paragraph 5, subparagraphs (a) 1 and 2 of the petition.

Denies generally and specifically each and every allegation contained in the petition of the above-named taxpayer not hereinbefore expressly admitted, qualified, or denied.

Wherefore, it is prayed that this appeal be denied.

E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue, Attorney for Respondent.

Of Counsel: E. L. Corbin, Special Attorney, Bureau of Internal Revenue.

BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

MOTION FOR LEAVE TO FILE AMENDMENT TO ANSWER—Filed July 26, 1935

Comes now the respondent, by his attorney, Robert H. Jackson, Assistant General Counsel for the Bureau of In-

CLERK'S COPY

In substantially the same manner the petitioner, on March 14, 1928, purchased 1,000 shares of the same stock with a loan from the First National Bank of Omaha and on March 20, 1928, he purchased 1,000 additional shares with a loan from the Omaha National Bank, the cost of each lot being $25,650. On April 13, 1928, the broker, on the petitioner's order, sold 2,000 shares for his account and on April 16, 1928, the petitioner got the identical certificates which he had put up as collateral at the banks when the shares were purchased and delivered them to the broker, receiving a check for the proceeds of the sale. One of the lots was sold for $29,310 and the other for $29,060.

On September 24, 1928, the petitioner instructed the broker to sell the remaining 1,000 shares of National Power & Light Co. stock, which he mistakenly thought was the balance in his trading account. In fact, there were only 900 shares in the trading account, being the same 900 shares that the petitioner had purchased in 1926. The broker, however, sold 1,000 shares for the petitioner's account, as he had been instructed to do, and notified the petitioner that his trading account was 100 shares short. The petitioner then instructed the broker to take 100 of the shares held in his collateral account and apply to the sale. The proceeds from the sale of the 1,000 shares were $39,835. The cost of the 900 shares [fol. 13] of trading stock was $21,150 and the cost of the 100 shares of collateral stock was $441.89.

On September 25, 1928, the petitioner purchased 2,000 shares of National Power & Light Co. stock for $84,375, and on October 2, 1928, 200 additional shares for $8,280, all of which he left in his trading account.

On December 31, 1928, the petitioner had on hand 800 shares in his collateral account and 2,200 shares in his trading account. He also had the 2,200 shares still on deposit as collateral at the Omaha National Bank and the 1,400 shares in his safety-deposit vault.

National Power & Light Co. Transactions of James E. Davidson in 1929

On January 3, 1929, the petitioner instructed the broker to sell 500 of the National Power & Light Co. shares in his trading account purchased September 25, 1928. On the same day the broker sold 500 shares for the petitioner's account

for $23,405 and, on petitioner's further instructions, purchased for his account 500 shares at a cost of $22,825.

On January 22, 1929, the petitioner instructed the broker to sell the 200 shares purchased on October 2, 1928. The broker sold 200 shares for petitioner's account on that day, the proceeds being $9,162. The profits on 100 of these shares belonged to another individual and were sent to him.

On January 28, 1929, the petitioner instructed the broker to sell 500 of the shares in his trading account purchased September 25, 1928, and also the 500 shares purchased January 3, 1929. On the same day the broker sold 1,000 shares for the petitioner's account for $53,785. Also, at about that time the petitioner took the remaining 1,000 shares in the trading account, purchased September 25, 1928, and deposited them as collateral on a loan at the Omaha National Bank. After these transactions there were no National Power & Light Co. shares left in the trading account. On February 11, 1929, the petitioner purchased through his trading account 600 shares for $31,905 and on February 15, 1929, he sold 600 shares for $32,871, leaving the trading account again exhausted.

On February 15, 1929, the petitioner withdrew the remaining 800 shares from the collateral account and put them in his safety-deposit vault with other securities. There were then no shares left in either the trading or the collateral accounts.

[fol. 14] All of the sales in 1929 up to this point were made through the trading account and the shares sold had never been issued to the petitioner but were held by the broker for his account in "street" names.

The next transaction in National Power & Light Co. stock occurred on March 27, 1929, when the petitioner purchased through the broker 1,000 shares with a part of the proceeds of a loan from the Omaha National Bank. Certificates for these shares numbered 80,250 to 80,258, inclusive, and 80,264 were delivered to the petitioner and put up as collateral with the bank as had been done in the previous transactions.

On June 19, 1929, the petitioner instructed the broker to sell 500 of the 1,000 shares purchased on March 27, 1929, certificates for which were on deposit at the Omaha National Bank. When the sale was made the petitioner called at the bank to get the certificates for delivery to the broker, but the bank refused to release them to the petitioner, stating

that they would make delivery themselves. The petitioner then instructed the bank to deliver 500 shares from the certificates numbered 80,250 to 80,258, inclusive, and 80,264. In making delivery of the certificates, however, a bank clerk, by mistake, delivered certificates from another lot which had been held as collateral by the bank since 1925. The mistake was not known by the petitioner at that time.

On July 1, 1929, the petitioner instructed the broker to sell the remaining 500 shares purchased on March 27, 1929. When this sale was made he instructed the bank to deliver to the broker certificates for 500 shares from the remainder of the certificates numbered 80,250 to 80,258, inclusive, and 80,264. Again, however, the bank made the same mistake and delivered to the broker certificates for 500 shares from the same lot which it had held as collateral since 1925. The selling price of the first 500-share lot sold by the broker on June 19, 1929, was $28,042.50 and of the second 500-share lot sold July 1, 1929, was $31,392.50. The cost of the 1,000 shares purchased by the petitioner on March 27, 1929, represented by certificates 80,250 to 80,258, inclusive, and 80,264, was $49,900. The cost of the 1,000 shares delivered to the broker by mistake was $4.42 per share or $4,420 for the 1,000 shares.

General Electric Co. Stock Transactions of James E. Davidson in 1929

On February 19, 1929, the petitioner, through his broker, purchased 100 shares of General Electric common for $22,[fol. 15] 705. A certificate for these shares, numbered 86,242, was received by the petitioner on March 4, 1929, and deposited as collateral with the Omaha National Bank, along with other collateral shares, to secure a loan of $147,000 which had been used to purchase these and other stocks. On March 26, 1929, the petitioner instructed his broker to sell the 100 shares purchased February 19, 1929. The broker sold the shares on that date and in completion of the sale the petitioner called at the bank and got the identical certificate numbered 86,242 which he had put up as collateral when the shares were purchased and delivered to the broker. The selling price of the 100 shares was $22,791. This was the petitioner's only transaction in General Electric Co. stock in 1929.

American Gas & Electric Co. Stock Transaction of Edith L. Davidson in 1929

On January 1, 1929, the petitioner, Edith L. Davidson, was the owner of 1,100 shares of American Gas & Electric Co. stock which she had purchased May 11, 1928, for $185,900. In purchasing these shares she had obtained a loan at the Omaha National Bank of $100,000, for which 700 of the shares were put up as collateral, and another loan from the First National Bank of $90,000, for which 400 shares were deposited as collateral. For each of these loans she executed a demand note in her own name. Certificates for the 1,100 shares purchased were delivered to her and deposited with the banks on July 6, 1928.

On January 2, 1929, a 52 per cent stock dividend was issued on the American Gas & Electric Co. stock and the petitioner received on her holdings 572 shares, which she placed in her safety-deposit vault. On January 10, 1929, the petitioner instructed the broker to begin selling the 1,672 shares which she then owned in 100 or 200-share lots so as not to break the market. Thereafter, the broker made sales as follows:

January 10, 1929	1,000 shares
January 16, 1929	500 shares
January 21, 1929	170 shares

The two remaining shares were not sold. The total proceeds of the sales were $246,340.70.

As the sales were made the certificates were taken from the banks and delivered to the broker. From the Omaha National Bank the petitioner got the identical certificates for the 700 shares that were on deposit there, but at the [fol. 16] First National Bank she was unable to get release of the certificates for the 400 shares there on deposit. The bank stated that it wanted to make its own delivery. In order to complete the transaction, however, the petitioner took from her safety-deposit vault certificates for 400 other shares of a previous stock dividend, together with 570 shares of the stock dividend of January 2, 1929, and delivered these certificates to the broker. When she received a check from the proceeds of these sales she paid off the loan at the First National Bank and got the certificates held by it, which she put in the safety-deposit vault in the place of the ones delivered to the broker.

The 400 shares which were taken from the safety-deposit vault for delivery to the broker were issued as a stock dividend on shares acquired by the petitioner previous to the purchase of the 1,100 shares on May 11, 1928, and had a cost to the petitioner of $27.50 a share. The cost of the 1,672 shares acquired by the purchase of the 1,100 shares on May 11, 1928, and the stock dividend of 572 shares on January 2, 1929, was about $109 each.

Opinion

Smith: The petitioners contend that the respondent has erroneously applied the first in, first out rule in computing their gains upon the above described sales of stock and that in each of the transactions involved the shares of stock sold were identified by their instructions to the broker to sell certain specified shares.

By amendments to his answers duly filed in each of the proceedings the respondent admits error in applying the first in, first out rule to the 400 shares of the American Gas & Electric Co. stock sold by Edith L. Davidson in 1929 and avers that such shares were identified by the certificates which the petitioner delivered to the broker in completion of the sale as those acquired by stock dividend, with a stipulated cost of $27.50 per share.

The respondent further avers that if the rule of first in, first out is held not applicable to the gains on the sale of certain of the shares of stock sold in 1928 and 1929 such gains are not taxable as capital net gains, as they were treated in the computation of the deficiencies herein, but are taxable as ordinary gains at the normal rate.

The respondent further avers in the amendment to his answer filed in Docket No. 72905 that, due to error in the computation of the deficiency therein asserted against Edith [fol. 17] L. Davidson, capital net gains were understated in the amount of $22,660.79.

For reasons hereinafter discussed we have found that the first in, first out rule is not applicable to any of the transactions involved in these proceedings, since in each transaction the shares sold were sufficiently identified. This ruling, however, does not dispose of the proceedings. We must still determine what shares were sold in each transaction and the amount of the profit or loss thereon.

The several transactions will be discussed in the order indicated in the above findings of fact.

National Power & Light Co. Transactions of James E. Davidson in 1928

As to the sale of the several lots of National Power & Light Co. shares in 1928, we think that there was an identification by the petitioner of all the shares sold and that the first in, first out rule is therefore inapplicable. The Commissioner's regulations, article 58 of Regulations 74, provide that this rule is to be applied only when the identity of the lots sold can not be determined. See Helvering vs. Rankin, 295 U. S. 123. In each of these sales the shares which the petitioner instructed the broker to sell had been bought and paid for by the petitioner and, with the exception of the 100 shares sold on September 24, 1928, the certificates for the shares had been issued to him. In each instance the petitioner instructed his broker to sell certain shares which he clearly identified by certificate numbers, and afterwards he delivered the shares so identified to the broker where they were not already in the broker's possession.

The respondent makes the argument that the evidence does not show that the broker actually sold the shares which the petitioner instructed him to sell or delivered to him for sale and that in fact the shares sold by the broker were all kept in "street" names and were not susceptible of identification. That is immaterial, we think. It is not identification by the broker, but the owner and seller of the shares, that is required. In Helvering vs. Rankin, supra, the Court said:

* * * It is true that certificates provide the ordinary means of identification. But it is not true that they are the only possible means. Compare Richardson vs. Shaw, 209 U. S. 365; 28 S. Ct. 512, 52 L. Ed. 835, 14 Ann. Cas. 981; Gorman vs. Littlefield, 229 U. S. 19; 33 S. Ct. 690, 57 L. Ed. 1047; Duel vs. Hollins, 241 U. S. 523, 36 S. Ct. 615, 60 L. Ed. 1143. Particularly is this so when, as here, [fol. 18] the thing to be established is the allocation of lots sold to lots purchased at different dates and different prices. The required identification is satisfied, if the margin trader has, through his broker, designated the securities to be sold as those purchased on a particular date and at a particular price. It is only when such a designation was not made at the time of the sale, or is not shown, that the "First-in, first-out" rule is to be applied.

The petitioner's instructions to the broker to sell certain specified shares and the subsequent delivery to the broker of certificates for the shares specified sufficiently identifies the shares sold.

National Power & Light Co. Transactions of James E. Davidson in 1929

As to the petitioner's 1929 transactions in the National Power & Light Co. stock a different situation is found. The first four sales in that year, 500 shares sold January 3, 200 shares sold January 22, 1,000 shares sold January 28, and 600 shares sold February 16, were all made through the petitioner's trading account with the broker, which was "long" at the time of the sales for the number of shares sold. No certificates for the shares sold had ever been issued to the petitioner. The shares were carried by the broker in "street" names and were not earmarked. In each instance the petitioner instructed the broker to sell certain shares purchased on a specified date. Under the decision of the Supreme Court in Helvering vs. Rankin, supra, that was a sufficient identification of the shares sold. Apparently, the transactions in Helvering vs. Rankin, supra, were conducted in substantially the same manner as the transactions here, since in both instances the shares sold had not been issued in the name of the customer or earmarked by the broker, but were held in "street" names.

In each of the two remaining sales in 1929, 500 shares sold June 19 and 500 sold July 1, the petitioner instructed the broker to sell certain shares represented by certificates which had been issued to him and were then being held by the bank as collateral on a loan. The petitioner expected to get these identical certificates from the bank and deliver them to the broker in completion of the sales, just as he had done in the 1928 sales, but through a mistake on the part of the bank other certificates, representing shares acquired at an earlier date, were delivered to the broker. In those circumstances, we think that the shares delivered to the broker were the shares actually sold by the petitioner. [fol. 19] In Miller vs. Commissioner (C. C. A., 2d Cir.), 80 Fed. (2d) 219, the rule pronounced in Helvering vs. Rankin, supra, was held to apply to transactions other than those conducted by a "margin trader." The fact there were that the broker, who had in his possession a number

of shares of stock which the taxpayer had purchased at different times and for different prices, was instructed to sell a certain number of shares from a specified lot, but instead sold and delivered to the purchaser shares from a different lot. The court held that the taxpayer's instructions to the broker to sell certain of the shares identified those shares as the ones sold, notwithstanding that the broker delivered other shares to the customer. In concluding its opinion, the court stated the three following rules:

* * * (1) that where there is no designation by the taxpayer at the time of making the sale, the certificate should be treated as the proper means for identification; (2) that a designation by instructions to the broker of the shares to be sold is controlling though the certificate delivered does not correspond with the instructions; (3) that the "First-in, first-out" rule applies only where there is neither identification by a certificate, nor by designation of the taxpayer.

In Uzal H. McCarter, 34 B. T. A.—(No. 81), the Board followed Miller vs. Commissioner, supra, with the qualification, however, that clause (2) of the above quotation from the court's opinion in that case should be construed to mean that a designation by instructions to the broker is controlling though the certificate delivered by the broker does not correspond with the instructions. Where the shares are already in the broker's possession there is nothing more for the seller to do after he instructs the broker to sell certain of those shares. Ordinarily, too, it is of no consequence to the broker or to the customer which shares are delivered by the broker. But as long as the petitioner has possession of the shares he is free to exercise his own choice and deliver whatever shares he may choose to in conclusion of the sale. In the instant case, for instance, the petitioner after instructing the broker to sell certain shares was free to change his mind about what shares he would dispose of and to deliver certificates for other shares. See also Horner vs. Commissioner, 72 Fed. (2d) 407, affirming 28 B. T. A. 360; Helen vs. Kelchner, 31 B. T. A. 262; George Vawter, 31 B. T. A. 884; affd.—Fed.—(C. C. A., 10th Cir., April 9, 1936). There is no suggestion in the Court's opinion in Helvering vs. Rankin, supra, that

the seller's instructions to the broker to sell certain shares would have prevailed as a means of identification over the fact of the delivery to the broker of certificates for other [fol. 20] shares, nor was this question presented by the facts in Miller vs. Commissioner, supra. In this case the delivery of the certificates by the petitioner or by the bank as his agent, we think, definitely identified the shares sold. The brokers sold the shares of stock represented by the certificates of indebtedness delivered—not those represented by some other certificates.

General Electric Co. Stock Transactions of James E. Davidson in 1929

The petitioner had only one completed transaction in General Electric Co. stock in 1929, involving the purchase of 100 shares on February 19 and the sale of those shares on March 26. The material facts with respect to the transaction are identical with those relating to the purchase and sale of the several lots of National Power & Light Co. stock in 1928. The petitioner received delivery of certificates for the shares purchased, deposited them with the bank as collateral on a loan, instructed the broker to sell those specific shares, and when the sale was made delivered the identical certificates to the broker in completion of the sale. The purchase price of the 100 shares was $22,705; the sale price $22,791, and the profit $86.

American Gas & Electric Co. Stock Transactions of Edith L. Davidson in 1929

The questions raised with respect to the transactions of Edith L. Davidson in American Gas & Electric Co. stock in 1929 have also been answered in our foregoing discussion of the sales of National Power & Light Co. shares by the petitioner, James E. Davidson, in 1929. There, other shares than those which the broker had been instructed to sell were delivered to him through a mistake on the part of the bank acting as agent for the petitioner. Here, other shares than those which the broker had been instructed to sell were delivered to him by the seller intentionally because she was unable to get possession of the shares which she had instructed the broker to sell. As to the identification of the shares sold there is no basis for a distinction in these transactions and, for the reasons already stated, we hold

that the shares sold were the shares actually delivered to the broker and not in part other shares which the seller instructed the broker to sell but did not deliver. We cannot sustain the petitioner's contention "that the delivery of a certificate other than the share representing that particular lot [which the broker was instructed to sell] because of inability to obtain the identical certificate from the bank [fol. 21] did not alter the transaction and that it still remained the sale of that specific lot."

With respect to the net capital gain question raised by the respondent in the amendments to his answers, it can be readily ascertained from the above stated facts whether the different lots of shares of stock sold by the petitioners in 1928 and 1929 had been held by them for a period of two years or more and therefore constituted capital assets within the meaning of section 101 of the Revenue Act of 1928. Where the shares sold had been held for less than two years the gains derived from such sales were not capital net gains, but were ordinary income taxable as such. Pursuant to the amended answers filed by the respondent the necessary adjustments in petitioners' tax liabilities will be reflected in the Rule 50 computations.

The further averment contained in respondent's amendment to his answer filed in Docket No. 72905 that Edith L. Davidson's net capital gains have been understated by the amount of $22,660.79 due to an error in the computation of the deficiency is supported by the evidence. The error appears on the face of respondent's Exhibit C. Adjustment in respect of this error likewise will be made in the Rule 50 computation.

Reviewed by the Board.

Judgment will be entered under Rule 50.

CONCURRING OPINION

MURDOCK Concurring:

The author of the prevailing opinion attempts to distinguish the present case from the Miller and McCarter cases on the ground that in the latter cases the delivery of the wrong certificate was made by the taxpayer's broker, while in the present case the wrong delivery was made either

ternal Revenue, and moves that leave be granted to file the attached amendment to the answer in order to make the pleadings conform to the proof.

Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue.

Of Counsel, E. C. Algire, Lloyd B. Harrison, Special Attorneys, Bureau of Internal Revenue.

Granted. Aug. 5, 1935.

Charles P. Smith, Member, U. S. Board of Tax Appeals.

[fol. 9] Before United States Board of Tax Appeals

[Title omitted]

Amendment to Answer—Lodged July 26, 1935, and Filed August 5, 1935

Comes now the respondent, by his attorney, Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue, and amends his answer to the petition by adding thereto the following alternative plea, preceding the prayer as contained therein:

Further answering the petition the respondent alleges in the alternative that if it be judicially determined from the evidence adduced in this proceeding that the 500 shares of National Power & Light Company stock sold on June 19, 1929, and the 500 shares of said stock sold on July 1, 1929, as shown by a summation of the testimony contained in Petitioner's Exhibit No. 3, represented 1000 shares of stock purchased by the petitioner on March 27, 1929, and if it be judicially determined from the evidence adduced that the 100 shares of General Electric Company stock sold on March 25, 1929, as shown by the summation of testimony contained in Petitioner's Exhibit No. 5, represented 100 shares of said stock acquired by petitioner on February 19, 1929, then and in that event it should be held that the profit on said sales of stock is not subject to the rate of tax prescribed by the capital net gain provisions of the Revenue Act of 1928 as determined by the respondent, as shown by Exhibit A and Schedules Nos. 1 and 3, of Respondent's Exhibit B, but

that such profit is subject to the normal and surtax rates prescribed by said revenue act.

Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue.

Of Counsel: E. C. Algire, Lloyd B. Harrison, Special Attorneys, Bureau of Internal Revenue.

[fol. 10] Before United States Board of Tax Appeals

Docket Nos. 61741, 72904, 72905

Promulgated May 8, 1936

James E. Davidson, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent

Edith L. Davidson, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent

Opinion

As applied to sales through a brokerage account of shares of stock purchased at different times and at different prices the first in, first out rule is not applicable:

(a) Where the seller ordered the broker to sell certain specified shares which had been issued to him and put up as collateral for a loan and in completion of the sale the seller delivered to the broker certificates for the identical shares. The certificates delivered to the broker identified the shares sold.

(b) Where the seller ordered the broker to sell certain specified shares which had not been issued to the seller but were held by the broker in a "street" name. The order to the broker to sell certain specified shares identified the shares sold. Helvering vs. Rankin, 295 U. S. 123.

(c) Where the seller ordered the broker to sell certain specified shares which had been issued to him and deposited

with a bank as collateral on a loan, but in completion of the sale the bank by mistake delivered to the broker certificates for other shares. The certificates delivered to the broker identified the shares sold.

(d) Where the seller ordered the broker to sell certain specified shares which had been issued to him and deposited with a bank as collateral on a loan, but in completion of the sale the seller, being unable to get possession of the shares specified, delivered certificates for other shares. The certificates delivered to the broker identified the shares sold.

Edward J. Svoboda, Esq., and J. A. C. Kennedy, Esq., for the petitioners.

E. C. Algire, Esq., for the respondent.

These proceedings are for the redetermination of deficiencies in petitioners' income taxes as follows:

[fol. 11]

Petitioner	Docket No.	Year	Deficiency
James E. Davidson	61741	1928	$2,609.47
Do	72904	1929	9,352.50
Edith L. Davidson	72905	1929	10,156.14

It is alleged that in his computation of each of the deficiencies the respondent erred in applying the rule of first in, first out in computing the profit on the sale of certain shares of stock. The proceedings were consolidated for hearing.

Findings of Fact

The petitioners, James E. Davidson and Edith L. Davidson, are husband and wife. James E. Davidson is president of the Nebraska Power Co. He began active trading in stocks in about 1925. He then owned a number of shares of National Power & Light Co. stock which he put up with the brokerage firm of Logan & Bryan, hereinafter sometimes referred to as the broker, with instructions that the shares were to be preserved "intact" and kept as his "estate" unless he specifically ordered them to be sold. He further instructed his broker that his active trading was to be done in other shares which he would purchase on margin or with funds borrowed from the banks.

The transactions in question in these proceedings were all conducted through the brokerage firm of Logan & Bryan

in the name of petitioner James E. Davidson. Both of the petitioners had other stock transactions during the years involved which are not in controversy.

National Power & Light Co. Transactions of James E. Davidson in 1928

On January 1, 1928, the petitioner, James E. Davidson, had in his brokerage account 900 shares of National Power & Light Co. stock designated as "collateral" stock which he had put up with the broker in 1925 and 900 other shares of the same stock designated as "trading" stock which he had purchased in 1926. The cost of the collateral stock was $4.42 per share and of the trading stock $23⅜ per share. In addition to those shares the petitioner had 2,200 shares of the same stock on deposit as collateral with the Omaha National Bank and 1,400 shares in a safety-deposit vault.

In January, 1928, the petitioner arranged with the Omaha National Bank for a loan of approximately $25,000 with which to purchase 1,000 additional shares of National Power & Light Co. stock, with the understanding that the shares [fol. 12] purchased would be deposited with the bank as collateral for the loan. On the petitioner's instructions the broker purchased for his account 1,000 shares on January 27, 1928, at a cost of $25,337.50. The certificates for 900 of those shares, numbered 27,417 to 27,425, inclusive, were delivered to the petitioner on February 8, 1928, and a certificate for the remaining 100 shares, numbered 27,556, was delivered to him on February 16, 1928. On those dates the petitioner deposited the certificates with the bank in accordance with his agreement.

On March 9, 1928, the petitioner ordered the broker to sell the 1,000 shares purchased on January 27, 1928, stating that he would get the certificates from the bank and deliver them as soon as the sale was made. On that date, March 9, 1928, the broker sold 1,000 shares for petitioner' account and in completion of the sale the petitioner, on March 9, 1928, got the identical certificates; numbered 27,417 to 27,425, inclusive, and 27,556, from the bank and delivered them to the broker. The petitioner then received a check from the broker in the amount of $26,310, representing the proceeds of the sale, which he deposited with the bank and paid off the loan.

was had thereon on July 8, 1936, at which time there was no appearance for the petitioner and the recomputation filed by the respondent was not contested. Wherefore, it is

Ordered and Decided that there is a deficiency in income tax due from the petitioner for 1929 in the amount of $5,139.20.

Eugene Black, Member. (Seal, U. S. Board of Tax Appeals 1924.)

Enter: Entered July 10, 1936.

[fol. 24] Before United States Board of Tax Appeals

[Title omitted]

Motion to Vacate Order of Redetermination and for Rehearing—Filed October 10, 1936

Comes now the petitioner by his attorney, Claude M. Houchins, and moves the Board to vacate and set aside its decision entered herein on July 10, 1936, and for rehearing and reconsideration upon the following grounds:

1. The decision is contrary to the evidence.

2. The opinion and decision are erroneous in law.

The facts upon which this motion is based are as follows:

For 1929, the Board erred in finding that the shares of National Power & Light Company stock delivered on June 19, and July 1, by the bank to the broker through mistake on the part of the bank, were the shares actually sold by the petitioner, and the Board also erred in finding that the bank was agent of the petitioner in making the delivery of the stock. The Board should have found that the shares ordered sold by the petitioner controlled as against the mistaken delivery by the bank.

Claude M. Houchins, 1001 15th St., N. W., Washington, D. C., Counsel for Petitioner.

Dated Oct. 12, 1936.

Charles P. Smith, Member U. S. Board of Tax Appeals.

[fol. 25] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

[Title omitted]

PETITION FOR REVIEW—Filed January 12, 1937

James E. Davidson, the petitioner in this case, hereby files his petition for review by the United States Circuit Court of Appeals for the Eighth Circuit, of a decision by the United States Board of Tax Appeals, promulgated on May 8, 1936, being 34 B. T. A. No. 83, redetermining a deficiency in the petitioner's income taxes for the calendar year 1929 in the amount of $5,129.20, and the petitioner respectfully shows:

I

The petitioner is an individual residing in the City of Omaha, County of Douglas, State of Nebraska, is a citizen of the said State of Nebraska, and filed his income tax return for the calendar year 1929 with the Collector of Internal Revenue for the Collection District of Nebraska.

II

The controversy involves the petitioner's liability for Federal income taxes for the calendar year 1929. The respondent originally determined and asserted a deficiency against this petitioner for the year 1929 in the amount of $9,352.50. The United States Board of Tax Appeals redetermined the deficiency for 1929 to be $5,129.20; of which redetermination this taxpayer seeks a review by this court.

On June 9, 1929, the petitioner ordered his broker to sell 500 shares of stock in the National Power and Light Company, instructing the broker specifically to sell 500 of 1,000 shares of such stock purchased on March 27, 1929. Certificates for such shares, numbered 80,250 to 80,258 inclusive, and 80,264, had been delivered to petitioner shortly after his purchase and had been deposited by the petitioner with the Omaha National Bank as collateral for a loan.

When the sale was made on June 19, 1929, the petitioner called at the Omaha National Bank to obtain certificates for [fol. 26] delivery to his broker, but the Bank refused to release the certificates to the petitioner, stating that the bank itself would make delivery to the broker. The petitioner then instructed the bank to deliver 500 shares from certi-

ficates numbers 80,250 to 80,258, inclusive, and 80,264. A bank clerk, admittedly by mistake, delivered certificates from another lot of similar stock, which lot had been held as collateral by the Bank since 1925; such mistake was not known to the petitioner at the time.

On July 1, 1929, the petitioner ordered his broker to sell the remaining 500 shares of the 1,000 shares of National Power and Light Company stock purchased on March 27, 1929. At the time the sale was made, the petitioner instructed the Omaha National Bank to deliver to his broker certificates for 500 shares from the remainder of the certificates numbered 80,250 to 80,258, inclusive, and 80,264. Again, however, the bank made the same mistake and delivered to the broker certificates for 500 shares from the same lot of similar stock which it had held as collateral since 1925. The selling price of the 500 shares sold on June 19, 1929, was $28,042.50, and of the second 500 shares sold July 1, 1929, was $31,392.50, totaling $59,435. The cost of the 1,000 shares purchased by the petitioner on March 27, 1929, represented by certificates numbered as above, was $49,900. The cost of the 1,000 shares originally represented by the certificates delivered by mistake to the broker by the bank was $4,420.

In his income tax return for 1929, the petitioner treated the 1,000 shares sold on June 19 and July 1, 1929, as consisting of the 1,000 shares purchased by him on March 27, 1929, at a cost of $49,900. The respondent determined the deficiency by applying the first-in-first-out rule. The Board of Tax Appeals held that the certificates delivered to the broker identified the shares sold, and that the gain from the sale of the 1,000 shares should be determined by comparing the selling price of $59,435 with the cost of the shares delivered to the broker for sale (under the Board's theory, $4,420) and computed the deficiency accordingly.

The final order of the Board determining the deficiency of $5,129.20 was entered on July 10, 1936. The petitioner filed with the Board of Tax Appeals on October 10, 1936, a motion to vacate the judgment of the Board and for rehearing; such motion was denied by an order of the Board entered October 12, 1936.

[fol. 27] III

The petitioner, being aggrieved by the findings of fact and constructions of law contained in the said findings and opin-

ion of the Board of Tax Appeals, and by its decision entered pursuant thereto, desires to obtain a review thereof by the United States Circuit Court of Appeals for the Eighth Circuit.

IV

The petitioner assigns as error the following acts and omissions of the Board of Tax Appeals:

(1) The holding that the delivery of certificates to his broker by petitioner or his agent, in itself alone, definitely identified the shares sold on June 19, and July 1, 1929.

(2) The holding that the delivery for sale of certificates for shares of stock to a broker by petitioner or his agent definitely identified the shares sold, notwithstanding petitioner's specific direction to his broker to sell shares purchased on March 27, 1929, and his specific directions to the Omaha National Bank to deliver to the broker certificates issued in respect of such shares.

(3) The failure to hold that in each of the sales of June 19 and July 1, 1929, petitioner's specific instructions to his broker to sell shares in the National Power and Light Company purchased on March 27, 1929, was sufficient in itself to identify the shares sold on such dates.

(4) The failure to hold that in each of the sales of June 19 and July 1, 1929, petitioner's specific instructions to his broker to sell and to the Omaha National Bank to deliver to his broker certificates issued in respect of shares in the National Power and Light Company purchased on March 27, 1929, were sufficient to identify the shares sold on such dates.

(5) The failure to hold that the petitioner's positive instructions to the Omaha National Bank to deliver in the case of each sale, shares from certificates numbered 80,250 to 80,258, inclusive, and 80,264, identified the blocks of 500 shares each sold on June 19 and July 1, 1929 as the shares purchased on March 27, 1929.

(6) The holding that the Omaha National Bank was the agent of the petitioner for the purpose of delivering shares to his broker, under the facts found by the Board of Tax Appeals.

(7) The holding that the petitioner was bound by the mistake of the Omaha National Bank in delivering to peti-

[fol. 28] tioner's broker certificates other than those which the bank was specifically ordered to deliver to carry out each of the sales of June 19 and July 1, 1929.

(8) The holding that the petitioner was bound by the mistake of his alleged agent, where such alleged agent failed and neglected to carry out the petitioner's specific instructions, in each of the sales of June 19 and July 1, 1929, to deliver to his broker certificates for 500 shares from those numbered 80,250 to 80,258, inclusive, and 80,264.

(9) The holding that the delivery by the Omaha National Bank, admittedly by error and contrary to the petitioner's specific instructions, of certificates issued in respect of shares acquired prior to March 27, 1929, identified the shares sold on June 19 and July 1, 1929, notwithstanding petitioner's express directions to his broker to sell the shares purchased March 27, 1929.

(10) The finding that the petitioner's instructions on June 19, 1929, to his broker to sell 500 of the shares purchased on March 27, 1929, did not identify the 500 shares sold on such date, where through error on the part of the Omaha National Bank, the certificates acquired by the petitioner in respect of stock purchased prior to March 27, 1929, were delivered to the broker.

(11) The finding that the petitioner's instructions on July 1, 1929, to his broker to sell the remaining 500 shares of the 1,000 shares purchased on March 27, 1929, did not identify the 500 shares sold on July 1, 1929, where certificates acquired by the petitioner in respect of stock purchased prior to March 27, 1929, were delivered by the Omaha National Bank to the petitioner's broker through error.

(12) The finding that the 500 shares of stock in the National Power and Light Company sold by the petitioner on June 19, 1929, were not part of the 1,000 shares purchased by the petitioner on March 27, 1929.

(13) The finding that the 500 shares of stock in the National Power and Light Company sold by the petitioner on July 1, 1929, were not the remaining portion of the 1,000 shares purchased by the petitioner on March 27, 1929.

(14) The finding that the 1,000 shares of stock in the National Power and Light Company sold by the petitioner in his two sales of June 19 and July 1, 1929, consisted of shares previously acquired by the petitioner and held by the Omaha National Bank as collateral since 1925.

[fol. 29] (15) The failure to find that the 1,000 shares of National Power and Light Company stock sold on June 19 and July 1, 1929, consisted of the 1,000 shares purchased by petitioner on March 27, 1929.

(16) The finding that the 1,000 shares of stock in the National Power and Light Company sold by the petitioner in his two sales of June 19 and July 1, 1929, had a cost or other basis to the petitioner for the purpose of determining gain or loss of $4,420, instead of $49,900.

(17) The finding of a deficiency for the year 1929 in the amount of $5,129.20, in lieu of a determination that there was no deficiency in income taxes due from the petitioner for the year 1929.

George Rogers, of Gardner, Morrison and Rogers, 1126 Woodward Building, Washington, D. C., Counsel for Petitioner.

Duly sworn to by George Rogers. Jurat omitted in printing.

IN UNITED STATES CIRCUIT COURT OF APPEALS

NOTICE OF FILING OF PETITION FOR REVIEW—Filed January 12, 1937

Mr. Morrison Shafroth, Assistant General Counsel for the Bureau of Internal Revenue, Washington, D. C.

Please take notice that the petitioner on the 12th day of January, 1937, A. D. filed with the clerk of the United States Board of Tax Appeals at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for [fol. 30] the Eighth Circuit of the decision of the United States Board of Tax Appeals heretofore rendered in the above entitled cause. A copy of the petition for review and the assignments of error as filed, is hereto attached and served upon you.

Done at Washington, D. C. this 12th day of January, A. D. 1937.

Respectfully, George Rogers, Counsel for Petitioner, Gardner, Morrison and Rogers, 1126 Woodward Building, Washington, D. C., of Counsel.

Personal service of the foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 12th day of January, A. D. 1937.

Morrison Shafroth, Chief Counsel for the Bureau of Internal Revenue, Counsel for Respondent.

BEFORE UNITED STATES BOARD OF TAX APPEALS

PRAECIPE FOR TRANSCRIPT OF RECORD—Filed March 5, 1937

To the Clerk of the United States Board of Tax Appeals:

You are hereby respectfully requested to prepare, certify, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Eighth Circuit, with reference to the petition for review heretofore filed by the petitioner in the above cause, a transcript of the record in the above cause prepared and transmitted as required by law and by the rules of the said Court, and to include in such transcript of record the following documents, or certified copies thereof, to-wit:

(1) The docket entries of all proceedings before the Board of Tax Appeals.

(2) Pleadings before the Board of Tax Appeals, as follows:

(a) The petition of James E. Davidson for redetermination of tax liability.

[fols. 31-32] (b) Answer of the respondent.

(c) Motion for leave to file amendment to answer and order of Board of Tax Appeals granting leave.

(d) Amendment to answer.

(3) Findings of fact and opinion of the Board of Tax Appeals.

(4) Order correcting the findings of fact of the Board of Tax Appeals.

(5) Decision of the Board of Tax Appeals.

(6) Motion to vacate and for rehearing, and order denying such motion.

(7) The petition for review filed by the petitioner in the above cause.

(8) The notice of filing petition for review, including acknowledgment of service of such notice and petition.

(9) This praecipe for record with acknowledgment of service thereon and date of filing.

George Rogers, Counsel for Petitioner.

Service of the above and foregoing praecipe and receipt of copy thereof are hereby acknowledged.

The foregoing praecipe for record is approved.

Morrison Shafroth, Chief Counsel, Bureau of Internal Revenue.

Clerk's certificate to foregoing transcript omitted in printing.

[fols. 33-34] Appearances of counsel omitted in printing.

[fol. 35] IN UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT

[Title omitted]

ORDER OF SUBMISSION—October 12, 1937

These causes, Nos. 10883 and 10884, having been called for hearing in their regular order, are argued together, and argument was commenced by Mr. E. J. Svoboda for petitioners, continued by Mr. Harry Marselli, Special Assistant to Attorney General, for respondent, and concluded by Mr. E. J. Svoboda for petitioners.

Thereupon, these causes were submitted to the Court on the transcripts of the records from said Board of Tax Appeals and the briefs of counsel filed herein.

[fol. 36] IN UNITED STATES CIRCUIT COURT OF APPEALS,
EIGHTH CIRCUIT, NOVEMBER TERM, A. D. 1937

No. 10,883

JAMES E. DAVIDSON, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

On Petition to Review Decision of United States Board of Tax Appeals

Mr. E. J. Svoboda (Mr. J. A. C. Kennedy, Mr. Yale C. Holland, Mr. G. L. DeLacy and Mr. R. E. Svoboda, on the brief) for Petitioner.

Mr. Harry Marselli, Special Assistant to the Attorney General (Mr. James W. Morris, Assistant Attorney General, and Mr. Sewall Key, Special Assistant to the Attorney General, on the brief) for Respondent.

Before Stone, Woodrough and Van Valkenburgh, Circuit Judges

OPINION—January 27, 1938

VAN VALKENBURGH, Circuit Judge, delivered the opinion of the court:

This case comes upon petition to review an order of redetermination of the Board of Tax Appeals whereby it was decided that there is a deficiency in income tax due from the [fol. 37] petitioner for 1929 in the sum of $5,129.50. The facts concerning the sale of stocks from which the questions here presented arise are thus found by the Board of Tax Appeals:

"On June 19, 1929, the petitioner instructed the broker to sell 500 of the 1,000 shares purchased on March 27, 1929, certificates for which were on deposit at the Omaha National Bank. When the sale was made the petitioner called at the bank to get the certificates for delivery to the broker, but the bank refused to release them to the petitioner, stating that they would make delivery themselves. The petitioner then instructed the bank to deliver 500 shares from the certificates numbered 80,250 to 80,258, inclusive, and 80,264.

In making delivery of the certificates, however, a bank clerk, by mistake, delivered certificates from another lot which had been held as collateral by the bank since 1925. Th mistake was not known by the petitioner at that time.

On July 1, 1929, the petitioner instructed the broker to sell the remaining 500 shares purchased on March 27, 1929. When this sale was made he instructed the bank to deliver to the broker certificates for 500 shares from the remainder of the certificates numbered 80,250 to 80,258, inclusive, and 80,264. Again, however, the bank made the same mistake and delivered to the broker certificates for 500 shares from the same lot which it had held as collateral since 1925. The selling price of the first 500-share lot sold by the broker on June 19, 1929, was $28,042.50 and of the second 500-share lot sold July 1, 1929, was $31,392.50. The cost of the 1,000 shares purchased by the petitioner on March 27, 1929, represented by certificates 80,250 to 80,258, inclusive, and 80,264, was $49,900. The cost of the 1,000 shares delivered to the broker by mistake was $4.42 per share or $4,420 for the 1,000 shares."

The facts thus found are undisputed, and from them it appears that the income profit on the shares sold over their cost is $55,015, and that such profit on the shares intended to be sold over their cost would have been $9,335. It is the contention of petitioner that the latter basis of computation should be employed, in which case there would be no deficiency in tax liability under returns made. The Board of Tax Appeals held that the shares delivered to the broker were the shares actually sold by the petitioner. The question presented for our answer is thus succinctly stated by government counsel:

[fol. 38] "Whether the taxable gain from the sale of 1,000 shares of certain stock in 1929 is to be determined, as the Board held, upon the basis of the cost of the shares which the taxpayer actually sold, as represented by the certificates actually delivered in consummating the sale, which certificates have been identified, rather than, as the taxpayer claims, upon the basis of the cost of the shares which he intended to sell and instructed the broker to sell."

It is the contention of the petitioner that the decisions of the Supreme Court and of the various Circuit Courts of Appeals have established as a matter of law that the taxpayer in all cases sufficiently identifies the shares to be sold when he designates such shares as being those purchased on a particular date. It is obvious, upon reading the decisions which the diligence of able counsel have cited for our consideration, that what superficially may appear to be divergent views are in most cases susceptible of reconciliation because of crucial differences in the situations presented. There are however a number of matters of law upon which there is substantial agreement. Concededly the decision of the Supreme Court in Helvering v. Rankin, 295 U. S. 123, is the pronouncement of that court which most materially affects the question here presented, and interpretations placed upon its language by the Circuit Courts of Appeals have largely been the basis of their rulings.

Treasury Regulation No. 74, Art. 58, provides that "when shares of stock in a corporation are sold from lots purchased at different dates and at different prices, and the identity of the lots cannot be determined, the stock sold shall be charged against the earlier purchases of such stock". In the Rankin case the petitioner was engaged in marginal transactions in none of which did the broker deliver to him, nor he to the broker, any stock certificate. The purchases and sales were made through the medium of street certificates handled by the broker, and the transactions were evidenced solely by debits and credits in the taxpayer's account on the broker's books. Through orders communicated to his broker he had made it plain that 1200 shares first purchased by him were in the nature of a permanent commitment on his part, and that the sales of stock incidental to his marginal transactions were to be consummated from stock later purchased. In this state of facts the Commissioner and Board concluded that it was impossible [fol. 39] to determine the identity of the lots purchased and sold, and that, consequently, the "First-in, first-out" regulation above quoted should be applied. The basis of the Commissioner's contention was that all the street certificates of stock held in the name of the broker were commingled and indistinguishable, and that, in such transactions, no certificate was issued in the name of the customer.

or earmarked for or otherwise allocated to him. Mr. Justice Brandeis said:

"The fallacy of this argument lies in the assumption that shares of stock can be identified only through stock certificates. It is true that certificates provide the ordinary means of identification. But it is not true that they are the only possible means. * * * The required identification is satisfied if the margin trader has, through his broker, designated the securities to be sold, as those purchased on a particular date and at a particular price. It is only when such a designation was not made at the time of the sale, or is not shown, that the First-in, first-out rule is to be applied."

Other matters were considered in this opinion, but the points ruled of interest here are that stock certificates, while the ordinary, are not the only possible, means of identification; and that the First-in, first-out rule applies in marginal transactions only when the identification of sales and purchases is not possible by any relevant evidence. In the instant case no marginal transactions are involved, and the "First-in, first-out" rule has no application. All the courts agree that the mere intention of the trader to sell particular shares without further identification is insufficient. Snyder v. Commissioner, 295 U. S. 134, 137; Vawter v. Commissioner, (C. C. A. 10) 83 F. (2d) 11; Horner v. Commissioner, (C. C. A. 3) 72 F. (2d) 407; Skinner, et al. v. Eaton, (C. C. A. 2) 45 F. (2d) 568. In Curtis v. Commissioner, 89 F. (2d) 736, this court had under consideration a case in which there was no mistake in the transaction as consummated. Everything was done under and in accordance with the desires of the petitioner who had the choice of so handling the matter that the transfer of stock could have been made from that acquired from a specific source. This court in that case recognized the certificate as the customary means of identification of stock in the following language:

"It may readily be conceded that certificates for stock are not the exclusive method of identifying stock dealt with, [fol. 40] but 'it is true that certificates provide the ordinary means of identification'." Citing Helvering v. Rankin, supra. It ventured no opinion as to the controlling effect of instructions if violated by a selling agent, and held that in the situation presented it must consider and follow what

by the taxpayer himself to the broker or by a bank to the broker. I do not agree that the difference in the facts is a sound basis for distinguishing the cases. A broker, just like a bank, is merely the agent of the seller, and where it appears, as it did in the Miller and McCarter cases, that the certificate actually delivered was identifiable as that pertaining to a different lot of stock from the one which the taxpayer designated for sale, there is just as good reason for holding the seller to the basis applicable to the shares represented by the certificate actually delivered as there is in the present case. I agree with the result reached in the present case because I think that identification by certificates is a better method of identification than identification by designation to the broker. See William W. Miller, [fol. 23] 31 B. T. A. 192, and my dissent in Usal H. McCarter, 34 B. T. A.—(No. 81).

McMahon and Turner agree with the above.

DISSENTING OPINION

ARUNDELL, Dissenting:

In the case of Usal H. McCarter, 34 B. T. A.—(No. 81), we definitely held that we would follow the rule laid down by the Second Circuit in Miller vs. Commissioner, 37 Fed. (2d) 213, to the effect that a designation to the broker of the shares to be sold is controlling although the certificate delivered does not correspond with the instructions given. I think we depart from that ruling in the instant case when we hold that the mistaken delivery by the banker of certain certificates shall prevail as an identification of what was intended to be sold over the very definite instructions of the owner to the contrary. The two rulings cannot be reconciled. We should adhere to the rule announced in Miller, supra.

Van Fossan, Mellott, and Arnold agree with this dissent.

(Seal, U. S. Board of Tax Appeals 1924.)

BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

ORDER AMENDING FINDINGS OF FACT

On motion of the respondent filed in these proceedings on May 23, 1936, the findings of fact contained in the Board's report promulgated May 8, 1936, are amended in the following respects:

The amount of $28,042.50 appearing in line 16, page 5, is changed to $28,142.50."

The words "her holdings" appearing on line 7, page 6, are changed to read "the 1,100 shares bought May 11, 1928."

The sentence beginning on line 23, page 6, is changed to read—

"In order to complete the transaction, however, the petitioner took from her safety deposit vault certificates for [fol. 23] 400 other shares received January 2, 1929, as stock dividend on stock of American Gas & Electric Company of a previous purchase, together with 570 shares received on the same date as stock dividend on the 1,100 shares of the said stock bought May 11, 1928, and delivered these certificates to the broker"

The word "thereon" is inserted between the words "dividend" and "of" appearing on page 6 in the last sentence of the last paragraph of the findings of fact.

Dated: June 15, 1936.

Charles P. Smith, Member. (Seal, U. S. Board of Tax Appeals 1924.)

CPS:aa.

BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

ORDER OF REDETERMINATION—July 10, 1936.

Pursuant to the findings of fact and opinion of the Board in the above-entitled proceeding promulgated May 8, 1936, the respondent, on June 12, 1936, filed a notice of settlement with statement of recomputation attached. Hearing

the taxpayer did and not what he might have done. Citing United States v. Safety Car heating Co., 297 U. S. 88, 96, and Bonham v. Commissioner, (C. C. A. 8) 89 F. (2d) 725.

In Vawter v. Commissioner, 83 F. (2d) 11, the Tenth Circuit Court of Appeals makes a similar reservation with respect to neglect or mistake on the part of a broker or selling agent, where different shares are delivered in violation of the taxpayer's intention and direction; but holds, in the case before it, that "it is well settled that, where a taxpayer has stock in his possession and deliberately delivers certain shares in consummation of a sale, he cannot afterwards say in computing income tax liability that he intended to sell other shares".

In Miller v. Commissioner, 80 F. (2d) 213, the Circuit Court of Appeals for the Second Circuit, in denying the application of the "First-in, first-out" rule, held that "a designation by instructions to the broker of the shares to be sold is controlling, though the certificate delivered does not correspond with the instructions", and that, where there is a designation such as was found sufficient in Helvering v. Rankin, supra, "it can make no difference whether the stock is held on margin or not". In that case the certificates were in the possession of the broker, who also held from the taxpayer written instructions to sell, embodying the number of shares and dates of purchase.

With the greatest respect for the eminent judges of the Second Circuit, we find ourselves unable to concur in the broad holding that a designation by instructions to the broker is controlling in all cases, though the certificate delivered does not correspond with the instructions. In the case at bar it is conceded that selling directions were given to the broker. It does not appear from the record that the instructions were written, as they were in the Miller case.

In our opinion the language used by Mr. Justice Brandeis in the Rankin case, in view of the situation there presented, fairly justifies the inference that identification by certifi- [fol. 41] cate is the best method where possible and available. This construction is especially applicable to the facts found in the present case, which differs in some phases from others brought to our attention. The certificates were in the possession of the taxpayer as between him and the broker, and the sale was to be consummated by their delivery.

Where such is the case the certificates, in the absence of special circumstances, not present here, should control as the best means of identification available. It should be noted that both the bank in which they were deposited, and the broker who made the sale were the agents of the taxpayer. The negligence alleged must be imputed to him. No responsibility attaches to the government. The result is that the taxpayer, while failing to realize the special benefit intended, has received the profit inuring from the sale actually made, while, if his present contention be indulged, the government has lost the income normally and legally taxable upon the transaction. It is uniformly held that tax liability must be determined by what in fact is done. United States v. Phellis, 257 U. S. 156, 172; United States v. Safety Car Heating Co., 297 U. S. 88, 96; Remington-Rand, Inc. v. Commissioner, (C. C. A. 2) 33 F. (2d) 77, 78; Bonham v. Commissioner, (C. C. A. 8) 89 F. (2d) 725, 728; Curtis v. Commissioner, (C. C. A. 8) 89 F. (2d) 736, 738; Horner v. Commissioner, (C. C. A. 3) 72 F. (2d) 407 and 78 F. (2d) 813. And this must be true if a dependable rule is to be established applicable to situations such as this.

While no ulterior purpose is to be attributed to the petitioner in this case, it is not difficult to perceive that the rule for which he contends may be made the means of tax evasion by collusion between taxpayer and broker. We do not mean to imply such contract in this case. The petitioner undoubtedly acted in good faith, and the broker presumably acted upon the certificates furnished for delivery in consummation of the sales. Notwithstanding the instructions given, the broker may well have assumed that the certificates furnished evidenced the final purpose of the trader. Compare Skinner v. Eaton, (C. C. A. 2) 43 F. (2d) 368, 370. The broker had no reason to suspect that the delivery of the certificates was not the deliberate act of petitioner, that being the adopted method of identifying the shares to be furnished in consummation of the sales.

[fol. 42] Being of opinion that the conclusion reached by the Board of Tax Appeals is fully supported by the facts found, its order of redetermination is

Approved and Affirmed.

[fol. 43] In United States Circuit Court of Appeals, Eighth Circuit

No. 10883

James E. Davidson, Petitioner,

vs.

Commissioner of Internal Revenue

Decree—January 31, 1938

On Petition to Review Decision of United States Board of Tax Appeals.

This cause came on to be heard on the petition to review an order of redetermination of the United States Board of Tax Appeals deciding there is a deficiency in the income tax due from the petitioner for the year 1929, and was argued by counsel.

On Consideration Whereof, It is now here ordered, adjudged and decreed by this Court that the order of redetermination of the said Board of Tax Appeals in this cause, be, and the same is hereby, approved and affirmed.

And it is further ordered by this Count that the petition to review herein, be, and the same is hereby, dismissed without the taxation of costs in favor of either of the parties in this Court.

January 31, 1938.

[fol. 44] In United States Circuit Court of Appeals, Eighth Circuit

[Title omitted]

Petition for Rehearing—Filed February 11, 1938

Comes now the Petitioner and moves the Court for an order setting aside the opinion and decision rendered in the above entitled case on the 27th day of January, 1938, and granting the Petitioner a rehearing for the following reasons:

I

The Court erred in holding that the certificates delivered to the broker by the Bank Clerk, through error and con-

trary to the instructions of the Petitioner, identified the [fol. 45] shares of stock sold by the Petitioner and were controlling as to such identification as against a specific designation by the Petitioner to sell on June 19 and July 1, 1929, the shares of stock purchased by the Petitioner on March 27, 1929.

II

The Court erred in holding that the Petitioner was b[illegible] by the mistake of the Bank Clerk and the broker in [illegible]livering and selling the certificates delivered through error by the Bank Clerk where the Petitioner had specifically instructed the Bank to deliver the certificates by designating certificate numbers representing stock purchased on March 27, 1929, and where the Petitioner by specific instructions to the broker ordered the sale of the shares of stock purchased by the Petitioner on March 27, 1929.

James E. Davidson, Petitioner. J. A. C. Kennedy, Yale C. Holland, G. L. DeLacy, E. J. Svoboda, R. E. Svoboda, Attorneys for Petitioner.

Attorney's Certificate

I, Edward J. Svoboda, certify that I am one of the attorneys for the Petitioner in the above case; that as such I have had charge of the trial and appeal of the said case on petition to review the decision of the United States Board of Tax Appeals and am familiar with all of the issues therein involved, and I further certify that the foregoing Petition for Rehearing is presented in good faith and not for the purposes of delay.

Edward J. Svoboda, One of the Attorneys for Petitioner.

[fol. 46] [File endorsement omitted]

In United States Circuit Court of Appeals

Order Denying Petition for Rehearing—February 22, 1938

The petition for rehearing filed by counsel for petitioner in this cause having been considered, It is now here ordered by this Court that the same, be, and it is hereby, denied.

In United States Circuit Court of Appeals

Motion to Stay Issuance of Mandate—Filed March 2, 1938

Now comes the Petitioner, James E. Davidson, and moves the Court to enter an order withholding and staying the mandate in the above entitled cause for the reason that it is the bona fide intention of the Petitioner to make proper application to the Supreme Court of the United States for a Writ of Certiorari in this case within the next sixty (60) days, and, in any event, without delay.

This Motion is made pursuant to the provisions of Section 350 of Title 28 of the United States Code to enable Petitioner to apply for and obtain a Writ of Certiorari from the Supreme Court of the United States.

The Petition for Certiorari will be filed and the Writ of Certiorari applied for for the reason that there is a diversity of decision, particularly between the Second Circuit of the United States Circuit Court of Appeals, and the Eighth Circuit of the United States Circuit Court of Appeals on the issues as presented in this case.

[fol. 47] The time to prepare, print and file such Petition for Certiorari in the Supreme Court of the United States has not yet elapsed and the Petitioner is reasonably certain that a Writ of Certiorari will be allowed and granted by the Supreme Court of the United States.

The Transcript of the record in this cause has been ordered from the Clerk of the United States Circuit Court of Appeals for the Eighth Circuit and the Petition for Certiorari is in the course of preparation and will be shortly submitted to the Clerk of the Supreme Court of the United States for printing, as soon as a transcript of the record can be obtained and appropriate page references inserted in the petition for Certiorari.

The affidavit of Edward J. Svoboda, one of the counsel for Petitioner, is filed herewith in support hereof.

James E. Davidson, by Kennedy, Holland, DeLacy & Svoboda, Edward J. Svoboda, His Attorneys.

AFFIDAVIT IN SUPPORT OF MOTION TO STAY MANDATE

UNITED STATES OF AMERICA,
State of Nebraska,
County of Douglas, ss:

Edward J. Svoboda, being first duly sworn upon his oath, deposes and says that he is one of the counsel for the Petitioner herein and that he prepared the Petitioner's Brief filed in this Court; that he is a duly licensed and practicing attorney at law; that the Motion for Re-hearing in this cause was overruled on February 22, 1938 and that unless the Motion to Stay Mandate of the Petitioner is allowed [fol. 48] and an order issued to stay and withhold the Mandate, pending the filing of a Petition for Certiorari to the Supreme Court of the United States, the Mandate of the United States Circuit Court of Appeals for the Eighth Circuit will issue on March 5, 1938; that the Petitioner does not have sufficient time to have the Transcript of Record in the above entitled matter printed and filed with the Clerk of the Supreme Court of the United States before the time for the issuance of such Mandate by the United States Circuit Court of Appeals for the Eighth Circuit unless the Motion for the staying and withholding of the said Mandate is allowed and order issued pursuant to such Motion; that it is the bona fide intention of the Petitioner to make application to the Supreme Court of the United States for a Writ of Certiorari within the time allowed by law and more specifically within at least sixty (60) days; that affiant has already ordered from the Clerk of the United States Circuit Court of Appeals for the Eighth Circuit a transcript of the record; that a Petition for Certiorari to the Supreme Court of the United States is in the course of preparation and awaits the record ordered from the Clerk of this Honorable Court for insertion of appropriate page references to the transcript of record; that the said Petition and the said Transcript will be filed without delay in the Supreme Court of the United States; that affiant believes that there is merit in the Petition for Writ of Certiorari and that the judgment of the United States Circuit Court of Appeals of the Eighth Circuit ought to be reversed by the Supreme Court of the United States; that the affiant believes that in equity and in justice, the mandate herein should be stayed until the Petitioner can, with all due

diligence, have completed the Transcript of Record and the Petition for Writ of Certiorari, and have the same filed with the Clerk of the Supreme Court of the United [fol. 49] States; that Petitioner should have a reasonable time, not exceeding sixty (60) days in which to prepare and file such Petition for Certiorari with the Transcript of the Record, and that the mandate herein should be stayed for a reasonable time, not in excess of sixty (60) days, to permit the cause to be transferred to the Supreme Court of the United States, and if the Writ of Certiorari is allowed and granted, such additional time until the cause is decided by the Supreme Court of the United States.

Edward J. Svoboda.

Subscribed and sworn to before me this 1st day of March, 1938. Dorothy Minturn, Notary Public. (Seal.)

[File endorsement omitted.]

In United States Circuit Court of Appeals

Order Staying Issuance of Mandate—March 3, 1938

On Consideration of the motion of petitioner for a stay of the mandate in this cause pending a petition to the Supreme Court of the United States for a writ of certiorari, It is now here ordered by this Court that the issuance of the mandate herein be, and the same is hereby, stayed for a period of thirty days from and after this date, and if within said period of thirty days there is filed with the Clerk of this Court a certificate of the Clerk of the Supreme Court of the United States that a petition for writ of certiorari, record and brief have been filed, the stay hereby granted shall continue until the final disposition of the case by the Supreme Court.

[fol. 50] Clerk's certificate to foregoing transcript omitted in printing.

[fol. 51] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed May 16, 1938

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Eighth Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 42,393. U. S. Circuit Court of Appeals, Eighth Circuit. Term No. 18. James E. Davidson, Petitioner, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed April 1, 1938. Term No. 18 O. T., 1938.

FILE COPY

Office - Supreme Court, U. S.
FILED
APR 1 1938
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

October Term, 1937

No. [redacted] 18

JAMES E. DAVIDSON,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT AND BRIEF IN SUPPORT THEREOF

J. A. C. KENNEDY,
YALE C. HOLLAND,
GEORGE L. DELACY,
EDWARD J. SVOBODA,
RALPH E. SVOBODA,
Counsel for Petitioner.

Law Briefs—OMAHA LINO-SLUG CO.—418 South 15th Street

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IN THE

Supreme Court of the United States

October Term, 1937

No.....

JAMES E. DAVIDSON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT AND BRIEF IN SUPPORT THEREOF

PETITION FOR WRIT OF CERTIORARI

James E. Davidson prays that a Writ of Certibrari issue to review the final judgment and decree of the United States Circuit Court of Appeals for the Eighth Circuit, entered in the above entitled cause on January 31, 1938 (R., p. 40), approving and affirming the order of redetermination of the Board of Tax Appeals in said cause (entered on July 10, 1936; R., p. 23), wherein the Board of Tax Appeals found a deficiency in income tax

due from the petitioner for the year 1929 in the amount of $5,129.20.

Statement of Facts

The petitioner had filed a petition to review an order of redetermination of the Board of Tax Appeals in the United States Circuit Court of Appeals of the Eighth Circuit, wherein the Board of Tax Appeals had determined a deficiency in income tax due from the petitioner for the year 1929 in the sum of $5,129.50, based upon the findings of fact of the Board of Tax Appeals, which are undisputed and are as follows:

> "On June 19, 1929, the petitioner instructed the broker to sell 500 of the 1,000 shares purchased on March 27, 1929, certificates for which were on deposit at the Omaha National Bank. When the sale was made the petitioner called at the bank to get the certificates for delivery to the broker, but the bank refused to release them to the petitioner, stating that they would make delivery themselves. The petitioner then instructed the bank to deliver 500 shares from the certificates numbered 80,250 to 80,258, inclusive, and 80,264. In making delivery of the certificates however, a bank clerk, by mistake, delivered certificates from another lot which had been held as collateral by the bank since 1925. The mistake was not known by the petitioner at that time.
>
> "On July 1, 1929, the petitioner instructed the broker to sell the remaining 500 shares purchased on March 27, 1929. When this sale was made he instructed the bank to deliver to the broker certificates for 500 shares from the remainder of the certificates numbered 80,250 to 80,258, inclusive, and 80,264. Again, however, the bank made the same mistake and delivered to the broker certificates for 500 shares from the same lot which it had held as collateral since

1925. The selling price of the first 500-share lot sold by the broker on June 19, 1929, was $28,042.50 and of the second 500-share lot sold July 1, 1929, was $31,392.50. The cost of the 1,000 shares purchased by the petitioner on March 27, 1929, represented by certificates 80,250 to 80,258, inclusive, and 80,264, was $49,900. The cost of the 1,000 shares delivered to the broker by mistake was $4.42 per share or $4,420 for the 1,000 shares."

(R., p. 14, and in decision of Circuit Court of Appeals, R., p. 35.).

The facts thus found are undisputed and from them it appears that the profit on the shares, which the petitioner ordered to be sold over their cost, would have been $9,335.00; whereas, the profit on the shares based on the certificates delivered by error by the bank to the broker is $55,015.00. It is the contention of the petitioner that the basis of computation of the profit should be upon the basis of the shares of stock ordered to be sold under instructions of the petitioner, and not upon the basis of the cost of the certificates delivered by the bank through error.

Question Presented

The question presented is therefore whether the taxable gain from the sale of 1,000 shares of the stock in 1929 is to be determined upon the basis of the cost of the shares which the petitioner had ordered and instructed the broker to sell, or upon the basis of the cost of the certificates delivered by the bank through error to the broker.

It is the contention of the petitioner that the decisions of the Supreme Court of the United States, and of the various Circuit Courts of Appeals, have established

as a matter of law that the taxpayer, and petitioner in this case, identified the shares to be sold when the petitioner designated such shares as being those purchased on a particular date, and when he instructed and ordered the broker to sell the shares so identified by the taxpayer and petitioner.

Reasons for Granting the Petition

1. The Circuit Court of Appeals erred in holding that the certificates of stock, delivered by error by the bank to the broker, identified the shares sold.

2. The Circuit Court of Appeals erred in not holding that where the taxpayer orders certain shares of stock sold, designating such shares by date of purchase, that such designation controls as against a mistaken delivery of certificates by a bank clerk.

3. The Circuit Court of Appeals erred in not holding that the basis of computing the gain on the stock sold was on the cost of the shares ordered sold and identified by purchase dates, and not on the basis of the cost of the certificates delivered by error by the bank clerk.

4. The Circuit Court of Appeals erred in not holding as a matter of law that petitioner's designation of shares to be sold by the broker sufficiently identified the shares sold, even though the bank clerk, through error, delivered certificates representing other shares to the broker.

5. The case raises an important question of Federal Law, which has been decided in other Circuit Courts of Appeals, and the decision of the Circuit Court of Appeals in this case is in conflict with the decision of the United

States Supreme Court and other Circuit Courts of Appeals on the same matter.

Helvering v. Rankin, 295 U. S. 123-134, 79 L. Ed. 1343.
Hobert v. Penrose, 38 Fed. (2d) 577 (C. C. A. 10).
Miller v. Comm. of Internal Revenue, 80 Fed. (2d) 219 (C. C. A. 2).
Fuller v. Comm. of Internal Revenue, 81 Fed. (2d) 176 (C. C. A. 1).
Milliken v. Comm. of Internal Revenue, 83 Fed. (2d) 213 (C. C. A. 2).
Kraus v. Comm. of Internal Revenue, 88 Fed. (2d) 616 (C. C. A. 2).

6. The principle involved is one of great general importance to the Government as well as the taxpayers, in that a definite yardstick, or rule, should be established by the United States Supreme Court, applicable to all jurisdictions, whereby the profit upon sale of shares of stock may be determined; that is, whether the designation of the shares to be sold by date of purchase, is to be used as a yardstick, or whether a delivery of other certificates (in this case through error of the bank clerk) is to be used as the basis for determining loss or gain.

7. In this case the Circuit Court of Appeals of the Eighth Circuit erroneously applied the rule, that the delivery of certificates, and the cost thereof, is controlling over a designation by the taxpayer to the broker of specific shares to be sold by dates of purchase, even though the certificates used were delivered by error of a bank clerk contrary to instructions of the petitioner.

8. The decision in this case is based upon a misconception of the rule laid down by the Supreme Court of

the United States in *Helvering v. Rankin*, 295 U. S. 123, and, using as the basis for its decision the cases of *Vawter v. Commissioner*, 83 Fed. (2d) 11 (C. C. A. 10); *Horner v. Commissioner*, 72 Fed. (2d) 407 (C. C. A. 3); *Skinner v. Eaton*, 45 Fed. (2d) 568 (C. C. A. 2); *Curtis v. Commissioner*, 89 Fed. (2d) 736 (C. C. A. 8); in all of which cases there was merely an intention to sell shares other than represented by certificates delivered; whereas, in the case at bar there was a specific designation of the shares to be sold by date of purchase—a specific designation and not only a secret or undisclosed intention.

Wherefore, it is respectfully submitted that this Petition for Writ of Certiorari, to review the judgment of the United States Circuit Court of Appeals, of the Eighth Circuit, should be granted.

J. A. C. Kennedy,
Yale C. Holland,
George L. DeLacy,
Edward J. Svoboda,
Ralph E. Svoboda,
Counsel for Petitioner.

BRIEF IN SUPPORT OF PETITION

Opinions of the Courts Below

The findings of fact, and the opinion, of the Board of Tax Appeals (R., pp. 10-16).

The Circuit Court of Appeals rendered an opinion on January 27, 1938 (R., p. 35), and also reported in 94 Fed. (2d) 300, *Davidson v. Comm. of Internal Revenue.*

Jurisdiction

The judgment of the Circuit Court of Appeals for the Eighth Circuit was entered on January 31, 1938 (R., p. 40). Petition for Rehearing overruled February 22, 1938.

The jurisdiction of this Court is invoked under Section 240 of the Judicial Code, as amended by the Act of February 13, 1925, 43 St. 938, 28 U. S. C. A., Sec. 347, page 359.

Statement

A statement of the facts is contained in the Petition for Writ of Certiorari and is incorporated herein by reference, but for sake of brevity will not be repeated nor enlarged upon.

Specifications of Error

The errors relied upon are indicated under "Reasons for Granting the Petition" in the Petition for Writ of Certiorari. They are incorporated herein by reference, but for sake of brevity are not repeated.

tificates delivered by employee of trust company were in most instances those owned by taxpayer before year 1913, rather than those deposited in 1916 and 1917, did not conclusively determine that taxpayer sold stock acquired before 1913."

In *Miller vs. Commissioner of Internal Revenue*, 80 F. (2d) 219 C. C. A. 2), decided December 9, 1935, we have a decision by the Circuit Court of Appeals which bears out every contention made by the petitioner herein, and we will quote from that decision because it answers every argument which the counsel for the Government made in connection with this matter before the Board of Tax Appeals, and which we believe is an answer to the decision of the Board of Tax Appeals in this case.

The Court in its syllabus said:

"2. Written instructions to broker to sell from taxpayer's safe-keeping account stock bought on specified date at designated price held sufficient identification for income tax purposes, of stock sold pursuant to that order, though order was fulfilled by delivery of certificates for stock purchased at earlier date.

"3. Certificate of stock delivered by broker should be treated as proper means for identification of stock sold for income tax purposes, where taxpayer makes no designation of particular stock at time of making sale.

"4. Taxpayer's designation, by instructions to broker concerning shares of stock to be sold, is controlling in identification of stock sold, for income tax purposes, though certificate delivered by broker does not correspond with instructions.

"5. 'First-in, first-out' rule for dentification of stock sold for income tax purposes, where taxpayer has purchased different lots of stock at different

times, applies only where there is no identification of stock sold by certificate delivered by broker or by taxpayer's designation."

In the body of the opinion the Court said:

"The decision of the Supreme Court in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. ed. 1343, shows that the 'First-in, First-out Rule' should not have been applied to the sale of this lot of stock where the customer had designated the shares to be sold as those purchased on a particular date and at a particular price. To be sure, the court there was dealing with the sale of corporate shares made through a broker which had been held in a marginal account with other lots of the same kind bought at different times and at different prices. But we cannot see why it should make a difference whether a broker has stock belonging to a customer in a safekeeping account or holds it as security for his advances. In each case the title is in the customer and if the broker has advanced money to purchase the stock he holds it only by way of pledge.'

"In Helvering v. Rankin, 295 U. S. 123, 128, 55 S. Ct. 732, 735, 79 L. Ed. 1343, Brandeis, J., said that: 'The required identification is satisfied, if the margin trader has, through his broker, designated the securities to be sold as those purchased on a particular date and at a particular price. It is only when such a designation was not made at the time of the sale, or is not shown, that the "First-in, First-out," rule is to be applied.'

"In Richardson v. Shaw, 209 U. S. 365, 378, 28 S. Ct. 512, 516, 52 L. Ed. 835, 14 Ann. Cas. 981, it was said that: 'A certificate of the same number of shares, although printed upon different paper and bearing a different number, represents precisely the same kind and value of property as does another certificate for a like number of shares of stock in the

same corporation. It is a misconception of the nature of the certificate to say that a return of a different certificate or the right to substitute one certificate for another is a material change in the property right held by the broker for the customer.'

"The certificates of stock involved in Richardson v. Shaw, 209 U. S. 365, 28 S. Ct. 512, 52 L. Ed. 835, 14 Ann. Cas. 981, had been held by a broker on margin and changed many times, and some of them had been released from pledge and delivered to the customer. The broker became bankrupt and his trustee sought to recover the shares which had been delivered to the customer on the ground that the delivery constituted an unlawful preference. The court held that there was no unlawful preference because a certificate of stock was not the property in the shares but only the evidence thereof and a return by the broker of a certificate different from the one purchased was not a material change in the property rights of the customer.

"The Commissioner relies on decisions of the Court of Appeals of the Third Circuit in Horner v. Commissioner of Internal Revenue, 72 F. (2d) 407, Commissioner of Internal Revenue v. Merchants' & Mfrs.' Fire Ins. Co., 72 F. (2d) 408, and Horner v. Commissioner of Internal Revenue, 78 F. (2d) 813, as showing that the certificate itself governs. But in each of these cases the taxpayer himself had custody of the certificates that he intended to sell, but delivered others to his broker without any special instructions as to the shares to be sold. It was held that intention alone, without designation, could not determine the shares sold. The same result was reached in Skinner v. Eaton, 45 F. (2d) 568 (C. C. A. 2).

"In Howbert v. Penrose, 38 F. (2d) 577, 68 A. L. R. 820, the Circuit Court of Appeals of the Tenth Circuit decided that book entries and a pocket memo-

randum kept by the taxpayer furnished sufficient identification, even though no designation of the shares to be sold was communicated to the broker. It is unnecessary for us to express any opinion as to the rule in such circumstances. We only hold that where there is a designation such as was found sufficient in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343, it can make no difference whether the stock is held on margin or not.

"This view carries out the purpose of the taxpayer, and we cannot see that it is contrary to sound public policy. If he had ordered a sale of 500 shares of Otis Elevator Stock without instructions as to dates of purchase, and after the sale had stated that he had intended to sell other shares than those evidenced by the certificates delivered, we should not regard his statement as a sufficient designation. But written instructions to sell embodying the number of shares and dates of purchase are an even more persuasive identification of the shares to be sold than the certificates which a broker may deliver without any thought about the particular lot he is selling. The identity of certificates frequently disappears in mergers, consolidations, or split-ups, and a single certificate may be issued in the place of various prior ones. A designation by the taxpayer of just the shares he is selling is often the best, if not the only available means he has for exercising his option to select the particular shares he desires to sell.

"It follows from the foregoing: (1) That where there is no designation by the taxpayer at the time of making the sale, the certificate should be treated as the proper means for identification; (2) that a designation by instructions to the broker of the shares to be sold is controlling though the certificate delivered does not correspond with the instructions; (3) that the 'First-in, First-out,' rule applies only where there is neither identification by a certificate, nor by designation of the taxpayer.

"The order of the Board of Tax Appeals is reversed, and the proceeding remanded, with direction to determine the amount of tax in accordance with the views we have expressed."

It will be noted here that a designation by instructions to the broker of shares to be sold is controlling, though the certificate delivered does not correspond with the instructions. There is no dispute in the Findings of Fact by the Board that the petitioner ordered the sale of specific stock purchased on a specific date. Therefore, in this case, the petitioner has complied with the requirement that he designate the specific stock to be sold, and having so designated it, without any question he is entitled to have the basis of any income tax computed upon the difference in cost between the stock ordered sold and the sale price thereof, without respect to the certificates delivered. The courts so recognize the rule.

In *Fuller vs. Commissioner of Internal Revenue*, 81 F. (2d) 176 (C. C. A. 1), decided January 7, 1936, the petitioner maintained account books showing the date of purchase of each lot of stock in the Packard Motor Car Company, the number of shares bought, the cost, date and amount of each stock dividend, the date of each sale, the number of shares sold, the sale price and the computation of the profit on each sale. Note that the instructions in this case were given by petitioner to his assistant to sell those shares which had cost the most and on which the taxable gain would be the least. The petitioner's assistant examined the ledgers and journals and ascertained therefrom those lots which he claimed were acquired at the highest prices and instructed the bookkeeper to sell the same. A broker was authorized to make the sales in small lots, and the entire 40,000

shares were sold in April of 1930. Broker sale slips were then recorded on the books. The Circuit Court of Appeals held that such instructions were sufficient to identify the stock sold, and in the syllabus said:

> "Where taxpayer, who maintained account book showing date of purchase of each lot of stock, number of shares bought, cost, date and amount of each stock dividend, date of each sale, number of shares sold, sale price, and computation of profits on each sale, instructed assistant to sell stock which had cost the most, 'First-in, First-out' rule held inapplicable in determining taxable gain, as against contention that stock sold could not be identified because taxpayer had received new certificates in stock split-up (Revenue Act, 1928, Paragraphs 22, 111, 112, 113)."

In the body of the opinion the Court said:

> "The Commissioner of Internal Revenue determined that the 25,000 shares thus sold could not be identified and that the provisions of the 'First-in, First-out' rule applied. The Board of Tax Appeals, differing from the Commissioner, adopted the view that the basis for determining the taxable gain derived from the sale of a portion of the stock received in a non-taxable exchange should be determined by apportioning the aggregate costs of all the shares owned by the taxpayer at the time of the exchange to the stock received by him in exchange. It should be said that when the Board of Tax Appeals rendered its decision, Helvering, Commissioner, v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343, indicating that certificates do not constitute the only possible means of identifying stock and holding that shares of stock held on margin and sold may be identified by 'designation' at the time of sale of what lots should be sold and what held, had not been decided. See, also, Miller v. Commissioner, 80 F. (2d) 219, decided December 9, 1935, by the Circuit Court of Appeals

for the Second Circuit. As to the view of the Board of Tax Appeals since the announcement of the Rankin decision, see Wieland v. Commissioner, Docket No. 73098 (decided October 10, 1935).

"When the taxpayer received certificates of stock in the 1929 'split-up,' so-called, his stockholder's interest in the corporation was not changed; it remained precisely what it had been. And the 25,000 shares sold were identified by his directions and by what was done pursuant to them with the specific lots of stock originally purchased in 1925, 1927, and 1928. The cost of such lots constituted the basis for determining the profit on the sale. This taxable gain was included in the taxpayer's return and the tax paid. In our opinion the Commissioner's determination of a deficiency based on the 'First-in, First-out' rule was, under the circumstances, unwarranted. So, too, as to the redetermination of a deficiency by the Board of Tax Appeals.

"The decision of the Board of Tax Appeals is reversed, and the case remanded to that Board, with instructions to reconsider the question before it in accordance with this opinion."

Note that in the foregoing case the designation by the petitioner was to petitioner's assistant, who, in turn, instructed the Petitioner's bookkeeper to sell the stocks which cost the most. In the instant case, the undisputed facts show that the petitioner instructed the broker to sell specific shares which had been purchased at a specific time. There can, therefore, be no question about the sufficiency of designation, and, as stated in the foregoing cases, the fact that other certificates were delivered does not change the order of sale or the shares sold.

In *Millikan vs. Commissioner of Internal Revenue*, 83 F. (2d) 213 (C. C. A. 2), decided April 6, 1936, the

facts sufficiently appear in the syllabus and in the opinion of the Court. It will be noted that the margin trader had on deposit with the broker certain shares which were held as collateral by the broker. Subsequent to that time, additional shares were purchased. It was the understanding that the collateral shares were not for sale, except on direction or to protect the account. An order was given to sell 600 shares, without further designation. The Court held that in view of the fact that the collateral shares were not to be sold, the 600 shares ordered sold were sold from the margin account. In the syllabus the Court said:

"1. That broker in confirmation of sale of stock ordered by margin trader had delivered certificates representing certain shares of stock deposited by such trader as collateral held not conclusive as to identity of shares sold for purpose of determining profit on sale for tax purposes, where there was undisputed evidence showing that other shares were actually sold.

"2. Where margin trader had at various times purchased shares of a particular stock and had deposited with broker other shares of same stock as collateral with understanding that collateral shares were not for sale except on direction or to protect account, shares sold when trader merely ordered sale of 600 shares held sufficiently identified for income tax purposes as shares sold on margin, in absence of direction to sell collateral or necessity for sale to protect account."

In the body of the opinion the Court said:

"The Commissioner based the deficiency on the theory that the broker delivered certificates representing certain shares of stock deposited as collateral and that this identified the shares sold. But this is not conclusive, for there is undisputed evidence show-

ing that other shares were sold. It was held in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 735, 79 L. Ed. 1343, that, when no certificate is issued to the customer or earmarked or otherwise allocated to him and all certificates for stock are in the name of the broker and are commingled and held by the broker for a common benefit of all dealing in that particular stock, there is no conclusive identification of the shares. The court pointed out that it was a fallacy to assume that the shares of stock can be identified only through stock certificates, saying: 'It is true that certificates provide the ordinary means of identification, but it is not true that they are the only means possible. * * * Particularly is this so when, as here, the thing to be established is the allocation of lots sold to lots purchased at different dates and different prices.'

"It was found by the Board, and it was undisputed, that the collateral stock was accepted by the brokers 'with the definite understanding that said securities are deposited as collateral and not for sale under any circumstances, except as a customer might direct or might be necessary for the protection of the account.' It is conceded that there was no instruction to the brokers to sell any of the collateral stock. Neither was there any sales necessary to protect the account because on that day the margin was ample. It is thus plain that the brokers had no option as to which class of stock was to be sold on petitioner's order. Within Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343, and Miller v. Commissioner, 80 F. (2d) 219 (C. C. A. 2), the petitioner has sufficiently established that the sales here were from the stocks held on margin. * * *".

It will be noted in the foregoing that the Court recognized the designation of stock to be sold because of an agreement or understanding that collateral stocks were not to be sold and that, therefore, the stock sold was the

stock in the margin account. In the case at bar, there was a specific designation of shares of stock to be sold, identified by date of purchase. What better designation could there be by the petitioner than such a specific lot?

In *Kraus vs. Commissioner of Internal Revenue*, 88 F. (2d) 616 (C. C. A. 2), decided March 8, 1937, the Court in its syllabus said:

"3. In taxation of gain on sale of stock, 'first-in, first-out rule' is applicable only, when there is no identification of shares sold with shares purchased, and although stock certificates are not the only means of identification and direction to broker to sell shares designated by date of purchase and price paid will be sufficient to establish identity of stock sold for determining cost basis, notwithstanding that broker actually delivers other certificates than those he was directed to sell, mere intention without more is not designation (Revenue Act 1928, par. 113 (a) (6), 26 U. S. C. A., par. 113 note)."

In the body of the opinion the Court said:

"It may be taken as established that if the petitioner were able to identfiy the stock he sold with any particular stock he acquired that he would be entiled to take the basis of that stock so identified as the basis of the shares sold. Section 113 (a) (6) Revenue Act of 1928, 26 U. S. C. A. par. 113 note. * * * He had the right to sell whatever stock he desired and the right of course to have the taxable gain, if any, computed on the basis of the cost of the particular shares which he elected to sell. * * * A direction to a broker to sell shares designated by date of purchase and price paid will be sufficient to establish identity of the stock sold for determining the cost basis of it even though the broker actually delivers other certificates than those he was directed to sell,

but intention without more is not designation. Miller v. Commissioner, 80 F. (2d) 219 (C. C. A. 2). See, also, Fuller v. Commissioner (C. C. A. 81 F. (2d) 176."

It will be noted that in the foregoing decision, the Court recognizes that the petitioner has the right to sell whatever stock he desires and that if he so designates the stock he desires to sell, such designation will be controlling, even though other certificates than those he directed to sell, are delivered.

II.

The Circuit Court of Appeals of the Eighth Circuit erred in basing its decision and judgment in the case upon decisions wherein a question of intention only was involved, and where there was no designation.

The decision of the Circuit Court of Appeals is to be found on page 35 of the Transcript of Record. It will be noted that in the opinion the Court said:

"All the courts agree that the mere intention of the trader to sell particular shares without further identification is insufficient. Snyder v. Commissioner, 295 U. S. 134, 137; Vawter v. Commissioner (C. C. A. 10), 83 F. (2d) 407; Skinner, et al. v. Eaton (C. C. A. 2), 45 F. (2d) 568. In Curtis v. Commissioner, 89 F. (2d) 736, this court had under consideration a case in which there was no mistake in the transaction as consummated. Everything was done under and in accordance with the desires of the petitioner who had the choice of so handling the matter that the transfer of stock could have been made from that acquired from a specific source. This court in that case recognized the certificate as the customary means of identification of stock in the following language:

"'It may readily be conceded that certificates for stock are not the exclusive method of identifying stock dealt with, but "it is true that certificates provide the ordinary means of identification." ' Citing Helvering v. Rankin, supra. It ventured no opinion as to the controlling effort of instructions if violated by a selling agent, and held that in the situation presented it must consider and follow what the taxpayer did and not what he might have done. Citing United States v. Safety Car Heating Co., 297 U. S. 88, 98, and Bonham v. Commissioner (C. C. A. 8), 89 F. (2d) 725."

It will be noted that all of the foregoing decisions deal with cases where there was a secret or undisclosed intention without designation.

The Circuit Court of Appeals, in dealing with the case of *Miller v. Commissioner*, 80 Fed. (2d) 219 (C. C. A. 2) (R., p. 38), says:

"In Miller v. Commissioner, 80 F. (2d) 219, the Circuit Court of Appeals for the Second Circuit, in denying the application of the 'First-in, first-out' rule, held that 'a designation by instructions to the broker of the shares to be sold is controlling, though the certificate delivered does not correspond with the instructions,' and that, where there is a designation such as was found sufficient in Helvering v. Rankin, supra, 'it can make no difference whether the stock is held on margin or not.' In that case the certificates were in the possession of the broker, who also held from the taxpayer written instructions to sell, embodying the number of shares and dates of purchase.

"With the greatest respect for the eminent judges of the Second Circuit, we find ourselves un-

Statutes Involved

The Statutes involved are as follows:

"Revenue Act of 1928, c. 852, 45 Stat. 791:

"Sec. 111. Determination Of Amount Of Gain Or Loss.

(a) Computation of gain or loss.—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.

* * * * *

"Sec. 113. Basis for Determining Gain or Loss.

(a) Property Acquired After February 28, 1913.—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; * * *"

ARGUMENT

I.

The Circuit Court of Appeals erred in failing to hold, as a matter of law, that the required identification of the shares sold was satisfied when the petitioner designated the securities to be sold as those purchased on a particular date, even though a bank employee, contrary to instructions, given by the taxpayer, delivered other certificates.

Law

The United States Supreme Court, and the various Circuit Courts of Appeal, have specifically passed upon

the question as to what constitutes a designation of certain stocks or shares when a sale is being ordered thereof and have specifically stated, as a matter of law, that the petitioner sufficiently identifies the shares to be sold when the petitioner designates such shares as being those purchased on a particular date.

The Supreme Court of the United States in *Helvering vs. Rankin*, 295 U. S. 123-134, 79 L. Ed. 1343, in the body of its opinion said:

> "* * * The fallacy of this argument lies in the assumption that shares of stock can be identified only through stock certificates. It is true that certificates provide the ordinary means of identification. But it is not true that they are the only possible means. Compare Richardson v. Shaw, 209 U. S. 365, 52 L. ed. 835, 28 S. Ct. 512, 19 Am. Bankr. Rep. 717, 14 Ann. Cas. 981; Gorman v. Littlefield, 229 U. S. 19, 57 L. ed. 1047, 33 S. Ct. 690, 30 Am. Bankr. Rep. 266; Duel v. Hollins, 241 U. S. 523, 60 L. ed. 1143, 36 S. Ct. 615, 37 Am. Bankr. Rep. 1. Particularly is this so when, as here, the thing to be established is the allocation of lots sold to lots purchased at different dates and different prices. The required identification is satisfied, if the margin trader has, through his broker, designated the securities to be sold as those purchased on a particular date and at a particular price. It is only when such a designation was not made at the time of the sale, or is not shown, that the 'First-in, first-out' rule is to be applied."

In *Howbert vs. Penrose*, 38 F. (2d) 577 (C. C. A. 10), the Court in its syllabus said:

> "2. Where taxpayer claimed that in selling shares of stock in 1918 he sold stock acquired in 1916 and 1917, and sustained loss on sale, proof that cer-

FILE COPY

Supreme Court of the United States

October Term, 1938

No. 43

JAMES S. DAVIDSON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE PETITIONER

J. A. C. Kraemer,
Van C. Hoskins,
Gilmore L. Dickey,
Edward J. Simmons,
Ralph E. Simmons,
Counsel for Petitioner.

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IN THE

Supreme Court of the United States

October Term, 1938

No. 18

JAMES E. DAVIDSON,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

This matter arises over an issue of deficiency in income taxes in which an opinion was rendered by the Board of Tax Appeals reported in 34 B. T. A. 555, which is also to be found at Record, page 9. The decision of the Circuit Court of Appeals of the Eighth Circuit is reported in 94 F. (2d) 300, under the title of *Davidson v. Commissioner of Internal Revenue*. The decision of

the Circuit Court of Appeals of the Eighth Circuit appears on page 32 of the Transcript of Record.

JURISDICTION

The decree sought to be reviewed was entered January 31, 1938 (R. p. 38). Petition for Rehearing was filed by the Petitioner on February 11, 1938 (R. p. 38) and the order denying the Petition for Rehearing was entered February 22, 1938 (R. p. 9). The Petition for Certiorari was filed April 1, 1938, and certiorari was granted May 16, 1938.

The jurisdiction of this Court is invoked under Sec. 240 of the Judicial Code as amended by the Act of February 13, 1925, 43 S. T. 938, 28 U. S. C. A., Sec. 347, page 359.

QUESTION PRESENTED

The question presented is whether the taxable gain from the sale of 1,000 shares of stock in National Power and Light Co. in the year 1929 is to be determined upon the basis of the cost of the shares which the Petitioner had ordered and instructed the broker to sell, or upon the basis of the cost of the certificates delivered by the bank, where the certificates were held as collateral, through error to the broker.

The Board of Tax Appeals, in its opinion and as affirmed by the Circuit Court of Appeals, held that the cost of the certificates delivered through error by the bank controlled.

The Petitioner contends that the cost of the shares ordered sold by him in the instructions to the broker controlled.

STATUTES INVOLVED

The Statutes involved are as follows:

"Revenue Act of 1928, c. 852, 45 Stat. 791:

"Sec. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) Computation of gain or loss.—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.

* * * * *

"Sec. 113. BASIS FOR DETERMINING GAIN OR LOSS.

(a) PROPERTY ACQUIRED AFTER FEBRUARY 28, 1913.—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; * * *"

STATEMENT OF CASE

The case arose out of the assessment of a deficiency in income taxes against the Petitioner as the result of transactions of James E. Davidson in 1929 in National Power and Light Co. Common Stock (R. pp. 12, 13, 14). There were other transactions in stocks involved in the trial before the Board of Tax Appeals, but no deficiency arose as the result of any of the other transactions

and, therefore, the questions involved before this Court will be limited to the question as to whether or not any deficiency in taxes resulted from the transactions of the Petitioner in National Power and Light Co. stock in 1929.

There is no dispute as to the facts in this case and the findings of the Board of Tax Appeals are accepted as the basis for the determination of this question by both the Petitioner and the Government. The findings of fact limited to the transactions involved in this case are as follows:

"The next transaction in National Power and Light Co. stock occurred on March 27, 1929, when the petitioner purchased through the broker 1,000 shares with a part of the proceeds of a loan from the Omaha National Bank. Certificates for these shares numbered 80,250 to 80,258, inclusive, and 80,264 were delivered to the petitioner and put up as collateral with the bank as had been done in the previous transactions.

"On June 19, 1929, the petitioner instructed the broker to sell 500 of the 1,000 shares purchased on March 27, 1929, certificates for which were on deposit at the Omaha National Bank. When the sale was made the petitioner called at the bank to get the certificates for delivery to the banker, but the bank refused to release them to the petitioner, stating that they would make delivery themselves. The petitioner then instructed the bank to deliver 500 shares from the certificates numbered 80,250 to 80,258, inclusive, and 80,264. In making delivery of the certificates, however, a bank clerk, by mistake, delivered certificates from another lot which had been held as collateral by the bank since 1925. The mistake was not known by the petitioner at that time.

"On July 1, 1929, the petitioner instructed the broker to sell the remaining 500 shares purchased on March 27, 1929. When this sale was made he instructed the bank to deliver to the broker certificates for 500 shares from the remainder of the certificates numbered 80,250 to 80,258, inclusive, and 80,264. Again, however, the bank made the same mistake and delivered to the broker certificates for 500 shares from the same lot which it had held as collateral since 1925. The selling price of the first 500-share lot sold by the broker on June 19, 1929, was $28,042.50 and of the second 500-share lot sold July 1, 1929, was $31,392.50. The cost of the 1,000 shares purchased by the petitioner on March 27, 1929, represented by certificates 80,250 to 80,258, inclusive, and 80,264, was $49,900. The cost of the 1,000 shares delivered to the broker by mistake was $4.42 per share or $4,420 for the 1,000 shares." (R. pp. 13, 14.)

The deficiency in the tax assessed by the Board arose out of the determination by the Board that the cost of the one thousand shares delivered to the broker by mistake was $4,420.00 for the one thousand shares, whereas, it is the contention of the Petitioner that the stock sold on June 19, 1929, and July 1, 1929, was the stock purchased on March 27, 1929, at a cost of $49,900.00.

ASSIGNMENTS OF ERROR

Assignment No. I

The Circuit Court of Appeals erred in holding that the certificates of stock, delivered by error, by the bank clerk to the broker, identified the shares sold.

able to concur in the broad holding that a designation by instructions to the broker is controlling in all cases, though the certificate delivered does not correspond with the instructions. In the case at bar it is conceded that selling directions were given to the broker. It does not appear from the record that the instructions were written, as they were in the Miller case."

It will therefore be seen that if the case at bar had been presented to the Circuit Court of Appeals of the Second Circuit, the contentions of the petitioner would have been sustained and no tax, or deficiency, would have been determined against the petitioner. The rule should be uniform, irrespective of what Circuit Court of Appeals of the United States the petitioner is compelled to resort to. The Petition for Writ of Certiorari should therefore be granted and allowed in order that a uniform rule may be established, and a conflict of decisions may be thereby avoided.

CONCLUSION

In view of the fact that the question here involved is one of great general importance, because of the conflict of decisions in the various Circuits governing like situations, and in view of the fact that under decisions laid down by the Circuit Courts of Appeals, under almost identical circumstances, no deficiency of income taxes would be assessable or determined against the petitioner, and because of such conflict in decisions and to establish a definite rule or yardstick, which both the Gov-

ernment and the taxpayers can follow, it is respectfully submitted that the Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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through stock certificates. It is true that certificates provide the ordinary means of identification. But it is not true that they are the only possible means. Compare Richardson v. Shaw, 209 U. S. 365, 52 L. ed. 835, 28 S. Ct. 512, 19 Am. Bankr. Rep. 717, 14 Ann. Cas. 981; Gorman v. Littlefield, 229 U. S. 19, 57 L. ed. 1047, 33 S. Ct. 690, 30 Am. Bankr. Rep. 266; Duel v. Hollins, 241 U. S. 523, 60 L. ed. 1143, 36 S. Ct. 615, 37 Am. Bankr. Rep. 1. Particularly is this so when, as here, the thing to be established is the allocation of lots sold to lots purchased at different dates and different prices. The required identification is satisfied, if the margin trader has, through his broker, designated the securities to be sold as those purchased on a particular date and at a particular price. It is only when such a designation was not made at the time of the sale, or is not shown, that the 'First-in, first-out' rule is to be applied."

In *Howbert vs. Penrose*, 38 F. (2d) 577 (C. C. A. 10), the Court in its syllabus said:

"2. Where taxpayer claimed that in selling shares of stock in 1918 he sold stock acquired in 1916 and 1917, and sustained loss on sale, proof that certificates delivered by employee of trust company were in most instances those owned by taxpayer before year 1913, rather than those deposited in 1916 and 1917, did not conclusively determine that taxpayer sold stock acquired before 1913."

In the body of the opinion, the Court said:

"In 1918, plaintiff decided to sell the stock acquired in 1916 and 1917, one of the reasons being to enable him to deduct a loss in his 1918 return. He sold the exact number of shares purchased in 1916 and 1917, at an actual loss of $54,030.75. That such was the stock sold is evidenced by the books of his office, and also a pocket memorandum kept by himself. These sales were effected, as were the pur-

chases, through the Colorado Springs office of a broker of the New York Stock Exchange. Delivery by the selling broker was affected by an order on the Columbia Trust Company. An employee of the trust company delivered, in most instances, certificates of the original stock owned by plaintiff, and not the certificates deposited in 1916 and 1917. The government declined to allow the loss incurred, but on the contrary charged plaintiff with a profit of $47,350.50, measured by the difference between the 1918 sale price and the 1913 value of the stock.

"The trial court found as a fact from the evidence, that 'plaintiff intended to and did sell' the shares acquired in 1916 and 1917. The finding is supported by the evidence, and cannot be disturbed. Dooley v. Pease, 180 U. S. 126, 21 S. Ct. 329, 45 L. Ed. 457; Stanley v. Supervisors of Albany County, 121 U. S. 535, 7 S. Ct. 1234, 30 L. Ed. 1000. The trial court likewise found:

"'It has since been ascertained that in the case of many such sales, the certificates so delivered by said depositary were certificates held by plaintiff on March 1, 1913, and in other cases plaintiff is unable to identify the certificates delivered by the depositary on such sales, as those received by it on the purchases above found. In one case only does the proof show that the certificates delivered on a sale were those actually received by the depositary on a purchase above found.'

"The contention of the collector is that the certificates delivered are conclusive as to the identity of the stock sold. Upon this, the trial court, in a memorandum opinion, said:

"'Where a party has held stock for many years, and later buys more, and in this case it is admitted that plaintiff bought a great deal more after 1913 than he sold in 1918, he has a right to decide which stock he is going to sell. The Government has not the

power to say that if the taxpayer sells any of his holdings in a particular company, it can say conclusively that he sold the stock bought at the cheapest price or the shares purchased before or after a certain date. He has the right to decide that himself.'

"In our opinion, proof of the certificates delivered does not conclusively determine what transaction did in fact take place. It is evidence, but not conclusive evidence. So it is of the question of intent of the seller, a point much labored at the trial and here; it is some evidence as to what was done, but not conclusive. The ultimate question is, what was done! It was, and must be readily conceded that if there had been a written contract of the sale of this stock, specifying 'the shares purchased by me in 1916,' and a clerk in the office of a trust company had delivered certificates acquired at an earlier date, the 'identity of the lot' could be and would be determined by the contract. There being no applicable statute of frauds, the finding of the trial court, upon ample evidence, identifies the lot as well as a written contract. * * *"

In *Miller vs. Commissioner of Internal Revenue*, 80 F. (2d) 219 (C. C. A. 2), decided December 9, 1935, we have a decision by the Circuit Court of Appeals which clears out every contention made by the Petitioner herein, and we will quote that decision because it answers every argument which the counsel for the Government made in connection with this matter before the Board of Tax Appeals, and which we believe is an answer to the decision of the Board of Tax Appeals in this case.

The Court in its syllabus said:

"2. Written instructions to broker to sell from taxpayer's safe-keeping account stock bought on specified date at designated price held sufficient identification for income tax purposes, of stock sold pursuant

to that order, though order was fulfilled by delivery of certificates for stock purchased at earlier date.

"3. Certificate of stock delivered by broker should be treated as proper means for identification of stock sold, for income tax purposes, where taxpayer makes no designation of particular stock at time of making sale.

"4. Taxpayer's designation, by instructions to broker concerning shares of stock to be sold, is controlling in identification of stock sold, for income tax purposes, though certificate delivered by broker does not correspond with instructions.

"5. 'First in first out' rule for identification of stock sold for income tax purposes, where taxpayer has purchased different lots of stock at different times applies only where there is no identification of stock sold by certificate delivered by broker or by taxpayer's designation."

The opinion of the Court is as follows:

"AUGUSTUS N. HAND, Circuit Judge.

"This appeal is from a decision of the United States Board of Tax Appeals. It contains a deficiency adjudged to exist in the income tax of the petitioner William W. Miller for the year 1929 arising out of a sale of 500 shares of common stock of Otis Elevator Company, and the dispute is over the proper identification of 300 of these shares, all 500 of which were sold from lots purchased at various times and various prices. The question before us is whether the 300 shares of stock might be identified for income tax purposes by oral and written instructions given by the taxpayer to his broker prior to sale specifying the shares to be sold by dates of purchase and original cost, or whether they could only be identified by the certificate themselves or under the 'First in First out Rule' set forth in section 58, Regulation 78.

"The taxpayer owned 1,735 shares of Otis Elevator common stock on February 25, 1929, which he had purchased at various dates and places. Each certificate was registered in the name of the taxpayer or in the name of Hallgarten & Co., who in general held the certificates for him in a safekeeping account. Whenever the taxpayer's account required additional margin Hallgarten & Co. would withdraw stock from the safekeeping account and place it with other stocks held by the latter as margin and, when no longer required as margin, would return it to the safekeeping account. In some instances this procedure resulted in the merger of certificates representing certain separate blocks. The taxpayer was not advised of these transactions in and out of the safekeeping account.

"On February 25, 1929, the taxpayer directed Hallgarten & Co. in writing to sell 500 shares of Otis Elevator common stock which had theretofore been purchased by them for his account. These shares were designated for sale in written instructions as follows:

100 shares bought March 6, 1926, at 121, $12,125.

100 shares bought March 8, 1926, at 120½, $12,075.

100 shares bought March 9, 1926, at 120¼, $12,050.

100 shares bought December 28, 1926, at 129½, $12,975.

100 shares bought December 28, 1926, at 129½, $12,975.

"There is no question about the identification of the stock bought March 8 and March 9, since the certificates delivered by Hallgarten & Co. were for the shares purchased on those dates. The 100 shares purchased March 6 and the 200 shares purchased

December 28, which were ordered sold, are the items in dispute.

"*The 100 Shares Bought March 6, 1926.*—The order for the sale of this stock was fulfilled by the delivery of certificate No. 6345 from block 6 containing 600 shares, which were registered in the name of Hallgarten & Co. The stock purchased March 6, 1926, had been commingled with the other shares in block 6 so that none of the certificates in the block were traceable to any particular purchase. The Commissioner, and on review the Board of Tax Appeals, applied the 'First in First out Rule' to the transaction, charged the 100 shares sold against the earliest purchases of such stock under article 58 of Regulations 74, instead of charging them against the purchase of March 6, 1926, and computed the profit accordingly for income tax.

"The decision of the Supreme Court in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. ed. 1343, shows that the 'First in First out Rule' should not have been applied to the sale of this lot of stock where the customer had designated the shares to be sold as those purchased on a particular date and at a particular price. To be sure, the court there was dealing with the sale of corporate shares made through a broker which had been held in a marginal account with other lots of the same kind bought at different times and at different prices. But we cannot see why it should make a difference whether a broker has stock belonging to a customer in a safekeeping account or holds it as security for his advances. In each case the title is in the customer and if the broker has advanced money to purchase the stock he holds it only by way of pledge.

"'The designation for sale of the 100 shares bought March 6, 1926, sufficiently identified that stock when sold and the cost of those shares reduced from the original price of $12,125 to the adjusted figure of $8,434.78, by allocation of a part of the cost to other

shares received as stock dividends, was the proper basis for computing any gain which the taxpayer realized from the sale. That figure, rather than $4,612.15 (the adjusted cost of 100 shares purchased March 31, 1934), which the Commissioner used under the 'First-in First-out' rule was the correct basis.

"In Helvering v. Rankin, 295 U. S. 123, 128, 55 S. Ct. 732, 735, 79 L. Ed. 1343, Brandeis, J., said that: 'The required identification is satisfied, if the margin trader has, through his broker, designated the securities to be sold as those purchased on a particular date and at a particular price. It is only when such a designation was not made at the time of the sale, or is not shown, that the "First-in, First-out" rule is to be applied.'

"*The 300 Shares Bought December 28, 1926.*— The order for the sale of this stock was fulfilled by the delivery of certificates Nos. 2694 and 2695 for 200 shares purchased on April 17, 1934, instead of by the delivery of certificates Nos. 3149 and 3152 issued for the stock purchased December 28, 1926, which was ordered sold. The Commissioner argued that these certificates issued for the stock purchased on December 28, 1926, alone represented that stock and neither the designation by the taxpayer of the shares he proposed to sell, nor the 'First-in, First-out' rule could affect the case. But the decisions of the Supreme Court in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343; Gorman v. Littlefield, 229 U. S. 19, 33 S. Ct. 690, 57 L. Ed. 1047; Richardson v. Shaw, 209 U. S. 365, 28 S. Ct. 512, 52 L. Ed. 835, 14 Ann. Cas. 981, and Duel v. Hollins, 241 U. S. 523, 527, 36 S. Ct. 615, 60 L. Ed. 1143, indicate that a designation made at the time of sale sufficiently identifies the stock.

"In Richardson v. Shaw, 209 U. S. 365, 378, 28 S. Ct. 512, 516, 52 L. Ed. 835, 14 Ann. Cas. 981, it was said that: 'A certificate of the same number of shares, although printed upon different paper and

bearing a different number, represents precisely the same kind and value of property as does another certificate for a like number of shares of stock in the same corporation. It is a misconception of the nature of the certificate to say that a return of a different certificate or the right to substitute one certificate for another is a material change in the property right held by the broker for the customer.'

"The certificates of stock involved in Richardson v. Shaw, 209 U. S. 365, 28 S. Ct. 512, 52 L. Ed. 835, 14 Ann. Cas. 981, had been held by a broker on margin and changed many times, and some of them had been released from pledge and delivered to the customer. The broker became bankrupt and his trustee sought to recover the shares which had been delivered to the customer on the ground that the delivery constituted an unlawful preference. The court held that there was no unlawful preference because a certificate of stock was not the property in the shares but only the evidence thereof and a return by the broker of a certificate different from the one purchased was not a material change in the property rights of the customer.

"The Commissioner relies on decisions of the Court of Appeals of the Third Circuit in Horner v. Commissioner of Internal Revenue, 72 F. (2d) 407, Commissioner of Internal Revenue v. Merchants' & Mfgrs.' Fire Ins. Co., 72 F. (2d) 408, and Horner v. Commissioner of Internal Revenue, 78 F. (2d) 813, as showing that the certificate itself governs. But in each of these cases the taxpayer himself had custody of the certificates that he intended to sell, but delivered others to his broker without any special instructions as to the shares to be sold. It was held that intention alone, without designation, could not determine the shares sold. The same result was reached in Skinner v. Eaton, 45 F. (2d) 563 (C. C. A. 2).

Assignment No. II

The Circuit Court of Appeals erred in not holding that where the taxpayer orders certain shares of stock sold, designating such shares by date of purchase, that such designation controls as to the cost of such shares sold as against the cost of certificates delivered by mistake by a bank clerk.

Assignment No. III

The Circuit Court of Appeals erred in not holding that the basis of computing the gain on the stock sold was the cost of shares ordered sold and identified by purchase dates, and not on the basis of the cost of certificates delivered by error by the bank clerk.

Assignment No. IV.

The Circuit Court of Appeals erred in not holding as a matter of law that Petitioner's designation of shares to be sold by the broker sufficiently identified the shares sold, even though the bank clerk, through error, delivered certificates representing other shares to the broker.

Assignment No. V

The Circuit Court of Appeals erred in holding that the delivery of certificates, and the cost thereof, is controlling over a designation by the taxpayer to the broker of specific shares to be sold by dates of purchase, even though the certificates used were delivered by error of a bank clerk contrary to instructions of the Petitioner.

Assignment No. VI

The Circuit Court of Appeals erred in affirming the decision of the Board of Tax Appeals holding that the

cost of the shares sold was determined by the certificates delivered through error by the bank clerk and not the cost of the shares purchased by the Petitioner on March 27, 1929.

Assignment No. VII

The Circuit Court of Appeals erred in holding that the Omaha National Bank was the agent of the Petitioner for the purpose of delivering shares to his broker, and that the Petitioner was bound, for tax purposes, by the mistake of the Omaha National Bank in delivering certificates other than those which the Petitioner ordered the bank to deliver to carry out each of the sales of June 19 and July 1, 1929.

Assignment No. VIII

The Court erred in finding that the one thousand shares of stock in the National Power and Light Co., sold by the Petitioner, in his two sales of June 19 and July 1, 1929, had a cost or other basis for the purpose of detremining gain or loss of $4,420.00 instead of $49,900.00.

Assignment No. IX

The Court erred in finding a deficiency as a matter of law for the year 1929 in the amount of $5,129.20 in lieu of a determination that there was no deficiency in income taxes due from the Petitioner for the year 1929.

ARGUMENT

Facts

As previously stated, the assessment of any deficiency in this matter arises out of the transactions of the Petitioner, James E. Davidson, in National Power and Light Company stock in 1929. All other transactions in stock involved in the appeal to the Board of Tax Appeals were decided by the Board of Tax Appeals as involving no additional deficiency. Therefore, the determination in this appeal involves only the National Power and Light Company transactions of the Petitioner in 1929.

Indeed, we do not have to concern ourselves with any of the transactions except the sale of $1,000 shares of National Power and Light Company stock, the history of which and the Findings of Fact relative to which are shown on page 13 of the Record, and, as previously stated, there is no dispute as to the Findings of Fact. It is the contention of the Petitioner that the law applied to such Findings of Fact creates no deficiency in tax to the Petitioner.

The Petitioner, Mr. James E. Davidson, had held National Power and Light Company stock for several years, and such stock had been put up as collateral to a bank loan and had been held by the bank as collateral since 1925 (Record, page 13). On March 27, 1929, the Petitioner purchased through the broker 1,000 shares of National Power and Light Company stock. The certificates representing this stock were those numbered 80,250 to 80,258, inclusive, and 80,264. It was necessary for the Petitioner to borrow a part of the proceeds from the bank to purchase this stock, and this loan was accomplished with The Omaha National Bank at the time of the purchase of these

1,000 shares. The Petitioner put up as collateral with the Bank the certificates numbered 80,250 to 80,258, inclusive, and 80,264 (Record, page 13). Therefore, up to this step, the identical certificates which represented the shares purchased on March 27, 1929, were held as collateral by The Omaha National Bank for the loan made by the Petitioner to purchase this stock.

There is no dispute under the Findings of Fact that on June 19, 1929, the Petitioner instructed the broker to sell 500 of the 1,000 shares purchased on March 27, 1929, certificates for which were on deposit at The Omaha National Bank. The Petitioner called at the Bank to get the certificates for delivery to the broker, but the Bank refused to release them to the Petitioner, stating that they would make delivery themselves. *It is further undisputed that the Petitioner then instructed the Bank to deliver 500 shares from the certificates numbered 80,250 to 80,258 inclusive, and 80,264, to the broker.* In making delivery of the certificates, however, a bank clerk, *by mistake,* delivered certificates from another lot which had been held as collateral by the Bank since 1925. *The mistake was not known by the Petitioner at that time* (Record, page 14). There is, therefore, no question but that the Petitioner instructed the broker to sell the specific shares purchased on March 27, 1929, which was represented by the certificates which were on deposit at The Omaha National Bank. It is the contention of the Petitioner that this is a specific designation of the shares to be sold.

On July 1, 1929, the Petitioner again instructed the broker to sell the remaining 500 shares purchased on March 27, 1929. When this sale was made, the Petitioner instructed the Bank to deliver to the broker certificates for

500 shares from the remainder of the certificates numbered 80,250 to 80,258, inclusive, and 80,264. Again, however, the Bank made the same mistake and delivered to the broker certificates for 500 shares from the same lot which it had held as collateral since 1925.

The selling price of the first 500 share lot sold by the broker on June 19, 1929, was $28,042.50, and of the second 500 share lot sold July 1, 1929, was $31,392.50. The cost of the 1,000 shares purchased by the Petitioner on March 27, 1929, represented by certificates 80,250 to 80,258, inclusive, and 80,264 was $49,900.00. The cost of the 1,000 shares delivered to the broker by the bank clerk by mistake was $4.42 per share, or $4,420.00 for the 1,000 shares. The deficiency assessed by the Board arises solely out of the profit computed by the Board as the difference between the $4,420.00 and the sale price of the two lots of stock on June 19, 1929, and July 1, 1929, for $59,435.00 (Record, page 14).

The Petitioner contends that under the decisions hereinafter cited he had designated to the broker the specific shares to be sold by amount and by date of purchase and that the shares sold by the broker were the shares which he had ordered the broker to sell. The Bank's error in delivering the wrong certificates did not in any manner affect the order which he had given to the broker to sell. As above stated, there is no dispute that such order was given by the Petitioner to the broker, that such designation was made by the Petitioner to the broker, that the Petitioner tried to get the identical certificates represented by the order to the broker, that the Bank refused to surrender the certificates but made its own delivery, that the Petitioner instructed the Bank to make the delivery of the shares from certificates num-

bered 80,250 to 80,258 and 80,264, and that the Bank clerk, in both instances, made a mistake by delivering other certificates and that this mistake was not known by or made known to the Petitioner.

Law

The United States Supreme Court, and the various Circuit Courts of Appeal, have specifically passed upon the question as to what constitutes a designation of certain stocks or shares when a sale is being ordered thereof and have specifically stated, as a matter of law, that the Petitioner sufficiently identifies the shares to be sold when the Petitioner designates such shares as being those purchased on a particular date.

The Supreme Court of the United States in *Helvering vs. Rankin*, 295 U. S. 123-134, 79 L. Ed. 1343, in its syllabus said:

> "I. As regard the application of the 'first-in, first-out,' regulation of the Treasury Department, relative to computing capital gains and losses for income tax purposes where shares of corporate stock are sold from lots purchased at different dates and at different prices and the identity of the lots cannot be determined, stock carried by a broker on margin for a customer is sufficiently identified by the customer's designating the securities to be sold as those purchased on a particular date at a certain price without identification of the stock certificates, which are carried without being earmarked, in the name of the broker or 'street names,' and have been commingled with like certificates held by the broker for other customers."

In the body of the opinion, the Court said:

> "* * * The fallacy of this argument lies in the assumption that shares of stock can be identified only

In *Millikan vs. Commissioner of Internal Revenue*, 83 F. (2d) 213 (C. C. A. 2), decided April 6, 1936, the facts sufficiently appear in the syllabus and in the opinion of the Court. It will be noted that the margin trader had on deposit with the broker certain shares which were held as collateral by the broker. Subsequent to that time, additional shares were purchased. It was the understanding that the collateral shares were not for sale, except on direction or to protect the account. An order was given to sell 600 shares, without further designation. The Court held that in view of the fact that the collateral shares were not to be sold, the 600 shares ordered sold were sold from the margin account. In the syllabus the Court said:

"1. That broker in confirmation of sale of stock ordered by margin trader had delivered certificates representing certain shares of stock deposited by such trader as collateral held not conclusive as to identity of shares sold for purpose determining profit on sale for tax purposes, where there was undisputed evidence showing that othen shares were actually sold.

"2. Where margin trader had at various times purchased shares of a particular stock and had deposited with broker other shares of same stock as collateral with understanding that collateral shares were not for sale except on direction or to protect account, shares sold when trader merely ordered sale of 600 shares held sufficiently identified for income tax purposes as shares held on margin, in absence of direction to sell collateral or necessity for sale to protect account."

In the body of the opinion the Court said:

"The Commissioner based the deficiency on the theory that the broker delivered certificates representing certain shares of stock deposited as col-

lateral and that this identified the shares sold. But this is not conclusive, for there is undisputed evidence showing that other shares were sold. It was held in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 735, 79 L. Ed. 1343, that, when no certificate is issued to the customer or earmarked or otherwise allocated to him and all certificates for stock are in the name of the broker and are commingled and held by the broker for a common benefit of all dealing in that particular stock, there is no conclusive identification of the shares. The court pointed out that it was a fallacy to assume that the shares of stock can be identified only through stock certificates, saying: 'It is true that certificates provide the ordinary means of identification, but it is not true that they are the only means possible. * * * Particularly is this so when, as here, the thing to be established is the allocation of lots sold to lots purchased at different dates and different prices.'

"It was found by the Board, and it was undisputed, that the collateral stock was accepted by the brokers 'with the definite understanding that said securities are deposited as collateral and not for sale under any circumstances, except as a customer might direct or might be necessary for the protection of the account.' It is conceded that there was no instruction to the brokers to sell any of the collateral stock. Neither was there any sales necessary to protect the account because on that day the margin was ample. It is thus plain that the brokers had no option as to which class of stock was to be sold on petitioner's order. Within Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343, and Miller v. Commissioner, 80 F. (2d) 219 (C. C. A. 2), the petitioner has sufficiently established that the sales here were from the stocks held on margin. * * *"

It will be noted in the foregoing that the Court recognized the designation of stock to be sold because of an agreement or understanding that collateral stocks were

not to be sold and that, therefore, the stock sold was the stock in the margin account. In the case at bar, there was a specific designation of shares of stock to be sold, identified by date of purchase. What better designation could there be by the Petitioner than such a specific lot?

In *Kraus vs. Commissioner of Internal Revenue*, 88 F. (2d) 616 (C. C. A. 2), decided March 8, 1937, the Court in its syllabus said:

"3. In taxation of gain on sale of stock, 'First-in First-out' rule is applicable only, when there is no identification of shares sold with shares purchased, and although stock certificates are not the only means of identification and direction to broker to sell shares designated by date of purchase and price paid will be sufficient to establish identity of stock sold for determining cost basis, notwithstanding that broker actually delivers other certificates than those he was directed to sell, mere intention without more is not designation (Revenue Act, 1928, par. 113 (a) (6), 26 U. S. C. A., par 113, note)."

In the body of the opinion the Court said:

"It may be taken as established that if the petitioner were able to identify the stock he sold with any particular stock he acquired that he would be entitled to take the basis of that stock so identified as the basis of the shares sold. Section 113 (a) (6), Revenue Act of 1928, 26 U. S. C. A., par 113 note. • • • He had the right to sell whatever stock he desired and the right of course to have the taxable gain, if any, computed on the basis of the cost of the particular shares which he elected to sell. • • • A direction to a broker to sell shares designated by date of purchase and price paid will be sufficient to establish identity of the stock sold for determining the cost basis of it even though the broker actually delivers other certificates than those he was directed

to sell, but intention without more is not designation. Miller v. Commissioner, 80 F. (2d) 219 (C. C. A. 2). See, also, Fuller v. Commissioner (C. C. A. 2), 81 F. (2d) 176."

It will be noted that in the foregoing decision, the Court recognizes that the Petitioner has the right to sell whatever stock he desires and that if he so designates the stock he desires to sell, such designation will be controlling, even though other certificates than those he directed to sell are delivered.

Property Right in Shares Sold May Be Identified By Designation of Date Purchased. Certificates Delivered Do Not Represent the Property Itself, But Merely the Evidence of It

In *Richardson v. Shaw*, 209 U. S. 365, 378, 28 S. Ct. 512, 516, 52 L. Ed. 835, 14 Ann. Cas. 981, the question arose whether the delivery of certificates by a broker to a customer amounted to a preference where the certificates delivered were other than those identifying the actual shares purchased by the customer. The Court, in an opinion by Justice Day, said:

"A certificate of the same number of shares, although printed upon different paper and bearing a different number, represents precisely the same kind and value of property as does another certificate for a like number of shares of stock in the same corporation. It is a misconception of the nature of the certificate to say that a return of a different certificate or the right to substitute one certificate for another is a material change in the property right held by the broker for the customer."

In *Gorman v. Littlefield*, 229 U. S. 19, 52 L. Ed. 1047 (1913), Justice Day, in referring to the case of *Richardson v. Shaw*, *supra*, said:

> "In Richardson v. Shaw, 209 U. S. 365, 52 L. Ed. 835, 28 Sup. Ct. Rep. 512, 14 Ann. Cas. 981, the nature of this property was the subject of discussion and decision in this court. In that case a broker, who had been adjudicated a bankrupt, shortly before the bankruptcy, and after his insolvency, turned over upon demand to a customer shares of stock similar to those which had been held for the customer, and for an equal number of shares. It was contended that, under the circumstances, this delivery of certificates amounted to a preference under the bankruptcy act. This court therefore had to consider the legal relation of customer and broker, in buying and holding shares of stock, and it was held that the certificates of stock were not the property itself, but merely the evidence of it, and that a certificate for the same number of shares represented precisely the same kind and value of property as another certificate for a like number of shares in the same corporation; that the return of a different certificate or the substitution of one certificate for another made no material change in the property right of the customer; that such shares were unlike distinct articles of personal property, differing in kind or value, as a horse, wagon, or harness, and that stock has no earmark which distinguishes one share from another, but is like grain of a uniform quality in an elevator, one bushel being of the same kind and value as another. It was therefore concluded that the turning over of the certificates for the shares of stock belonging to the customer, and held by the broker for him, did not amount to a preferential transfer of the bankrupt's property."

Therefore, applying the foregoing law to the present situation, the petitioner ordered the sale of the shares

of stock which he had purchased on March 27, 1929. He had a property right in these shares and it was such property right which he ordered and directed the broker to sell. It was that property right in these shares which he did sell. The certificates were merely evidence of that property right. They did not change that property right and it was still that property right in the shares purchased on March 27, which he sold, even though certificates other than those which represented the purchase of the shares on March 27, 1929, were delivered to consummate the sale.

True Facts, When Found, Take Precedence Over Any Rule

It will be noted in this case that the undisputed fact is that the petitioner ordered the sale of the shares of stock which he purchased on March 27, 1929. No one contends that there was any deceit of the Court on the part of the petitioner in claiming that he ordered the sale of the shares purchased on March 27, 1929. This, therefore, amounts to a finding of the true facts.

In *Rankin v. Commissioner of Internal Revenue*, 84 F. (2d) 551 (C. C. A. 3), the question arose as to the application of the "First-in, First-out" rule. In stressing the consideration to be given to the *true facts*, the Court said:

> "The difference between the taxpayer and the board is that the former reaches the conclusion that the shares directed to be sold were designated and identified as the shares purchased in 1928; the latter views the direction given as merely the declaration of an intention to retain 1,200 shares indifferent as to what shares and without identifying the shares

to be sold. This difference the Supreme Court characterized as 'obviously vital.'

"The view of the board, whether called an expression of opinion or the statement of a conclusion, or, if the expression be preferred, an ultimate fact finding, has in it all the elements of a conclusion of law. Under the evidentiary facts as found, the board concludes that the 'First-in, First-out' rule applies. This is a conclusion of law. The board agrees to the proposition, which is an undisputed one, that if the evidence indicates what shares were sold, the rule does not apply. In reaching the conclusion at which the board arrived, its attention was directed solely to the feature, which it emphasizes, that at the time the sale was directed the shares to be sold were not identified. This overlooks the important, and it seems to us controlling, feature that the designation of what shares were not to be sold was a designation and identification of what were to be sold. The taxpayer owned 2,500 shares. Of these 1,200 had been bought in 1926 with his father's money. These he had directed were not to be sold. There were other shares bought in 1928. When therefore he directed 1,300 shares to be sold, as the 1,200 shares bought in 1926 were not to be sold, his direction was to sell the other stock bought in 1928. It follows that the evidence identifies the stock sold and the rule applied by the board is not applicable."

Therefore, the thing to be determined is the fact, and the fact is undisputed in this case. If the evidence, therefore, discloses what the true fact is, the presumed fact yields to this.

The Circuit Court of Appeals, in its decision (R. p. 37), says:

"While no ulterior purpose is to be attributed to the petitioner in this case, it is not difficult to

perceive that the rule for which he contends may be made the means of tax evasion by collusion between taxpayer and broker."

If, therefore, the Petitioner has established the true t and which is undisputed, why should this Petitioner penalized in being called upon to pay additional in- he taxes just because someone else might use the rule evade taxes if the Government was not sufficiently gent to ascertain what the true fact was?

nk Was Not Agent in Making livery of Certificates

The Circuit Court of Appeals, in its opinion (R. p. , states that the bank in which the certificates were posited as collateral, and the broker who made the sale, re the agents of the taxpayer. The bank was not an nt of the taxpayer in the transaction. The bank had roperty right in any certificates which it held as col- eral. The Petitioner called for the certificates to make livery of them to the broker. The bank refused to let Petitioner take the certificates, saying to the Peti ner that the bank would make its own delivery to pro- t the lien right which they had upon the shares of ck as collateral. This does not change the fact that shares of stock ordered sold were specifically desig- ted as those purchased on March 27, 1929. That was e contract with the broker and it was that contract ich was being carried out. No change was ever made that contract. The certificates were merely evidence the property right and not the property itself. The nk was therefore delivering, not as agent of the Peti- ner, but in the protection of its own lien, the certificates ich they erroneously delivered.

"In Howbert v. Penrose, 38 F. (2d) 577, 68 A. L. R. 820, the Circuit Court of Appeals of the Tenth Circuit decided that book entries and a pocket memorandum kept by the taxpayer furnished sufficient identification, even though no designation of the shares to be sold was communicated to the broker. It is unnecessary for us to express any opinion as to the rule in such circumstances. We only hold that where there is a designation such as was found sufficient in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343, it can make no difference whether the stock is held on margin or not.

"This view carries out the purpose of the taxpayer, and we cannot see that it is contrary to sound public policy. If he had ordered a sale of 500 shares of Otis Elevator Stock without instructions as to dates of purchase, and after the sale had stated that he had intended to sell other shares than those evidenced by the certificates delivered, we should not regard his statement as a sufficient designation. But written instructions to sell embodying the number of shares and dates of purchase are an even more persuasive identification of the shares to be sold than the certificates which a broker may deliver without any thought about the particular lot he is selling. The identity of certificates frequently disappears in mergers, consolidations, or split-ups, and a single certificate may be issued in place of various prior ones. A designation by the taxpayer of just the shares he is selling is often the best if not the only available means he has for exercising his option to select the particular shares he desires to sell.

"It follows from the foregoing: (1) That where there is no designation by the taxpayer at the time of making the sale, the certificate should be treated as the proper means for identification; (2) that a designation by instructions to the broker of the shares to be sold is controlling though the certificate delivered does not correspond with the instructions; (3)

that the 'First-in, First-out' rule applies only where there is neither identification by a certificate, nor by designation of the taxpayer.

"The order of the Board of Tax Appeals is reversed, and the proceeding remanded, with direction to determine the amount of tax in accordance with the views we have expressed."

It will be noted here that designation by instructions to the broker of shares to be sold is controlling, though the certificate delivered does not correspond with the instructions. There is no dispute in the Findings of Fact by the Board that the Petitioner ordered the sale of specific stock purchased on a specific date. Therefore, in this case, the Petitioner has complied with the requirement that he designate the specific stock to be sold, and having so designated it, without any question he is entitled to have the basis of any income tax computed upon the difference in cost between the stock ordered and the sale price thereof, without respect to the certificates delivered. The courts so recognize the rule.

In *Fuller vs. Commissioner of Internal Revenue*, 81 F. (2d) 176 (C. C. A. 1), decided January 7, 1936, the Petitioner maintained account books showing the date of purchase of each lot of stock in the Packard Motor Car Company, the number of shares bought, the cost, date and amount of each stock dividend, the date of each sale, the number of shares sold, the sale price and the computation of the profit on each sale. Note that the instructions in this case were given by Petitioner to his assistant to sell those shares which had cost the most and on which the taxable gain would be the least. The Petitioner's assistant examined the ledgers and journals and ascertained therefrom those lots which he claimed were acquired at

the highest prices and instructed the bookkeeper to sell the same. A broker was authorized to make the sales in small lots, and the entire 40,000 shares were sold in April of 1930. Broker sales slips were then recorded on the books. The Circuit Court of Appeals held that such instructions were sufficient to identify the stock sold, and in the syllabus said:

> "Where taxpayer, who maintained account book showing date of purchase of each lot of stock, number of shares bought, cost, date and amount of each stock dividend, date of each sale, number of shares sold, sale price, and computation of profits on each sale, instructed assistant to sell stock which had cost the most, 'first-in, first-out' rule held inapplicable in determining taxable gain, as against contention that stock sold could not be identified because taxpayer had received new certificates in stock split-up (Revenue Act 1928, Paragraphs 22, 111, 112, 113)."

In the body of the opinion the Court said:

> "The Commissioner of Internal Revenue determined that the 25,000 shares thus sold could not be identified and that the provisions of the 'first-in, first-out' rule applied. The Board of Tax Appeals, differing from the Commissioner, adopted the view that the basis for determining the taxable gain derived from the sale of a portion of the stock received in a non-taxable exchange should be determined by apportioning the aggregate costs of all the shares owned by the taxpayer at the time of the exchange to the stock received by him in exchange. It should be said that when the Board of Tax Appeals rendered its decision, Helvering, Commissioner, v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343, indicating that certificates do not constitute the only possible means of identifying stock and holding that shares of stock held on margin and sold may be identified by 'desig-

nation' at the time of sale of what lots should be sold and what held, had not been decided. See, also, Miller v. Commissioner, 80 F. (2d) 219, decided December 9, 1935, by the Circuit Court of Appeals for the Second Circuit. As to the view of the Board of Tax Appeals since the announcement of the Rankin decision, see Wieland v. Commissioner, Docket No 73098 (decided October 10, 1935).

"When the taxpayer received certificates of stock in the 1929 'split-up,' so called, his stockholder's interest in the corporation was not changed; it remained precisely what it had been. And the 25,000 shares sold were identified by his directions and by what was done pursuant to them with the specific lots of stock originally purchased in 1925, 1927, and 1928. The cost of such lots constituted the basis for determining the profit on the sale. This taxable gain was included in the taxpayer's return and the tax paid. In our opinion the Commissioner's determination of a deficiency based on the 'first-in, first-out' rule was, under the circumstances, unwarranted. So, too, as to the redetermination of a deficiency by the Board of Tax Appeals.

"The decision of the Board of Tax Appeals is reversed, and the case remanded to that Board, with instructions to reconsider the question before it in accordance with this opinion."

Note that in the foregoing case the designation by the Petitioner was to Petitioner's assistant, who, in turn, instructed the Petitioner's bookkeeper to sell the stocks which cost the most. In the instant case, the undisputed facts show that the Petitioner instructed the broker to sell specific shares which had been purchased at a specific time. There can, therefore, be no question about the sufficiency of designation, and, as stated in the foregoing cases, the fact that other certificates were delivered does not change the order of sale or the shares sold.

Contract With Broker Not Required to Be in Writing

The Circuit Court of Appeals (R. p. 36) said:

> "In the case at bar it is conceded that selling directions were given to the broker. It does not appear from the record that the instructions were written, as they were in the Miller case."

There is no question that there was no applicable statute of frauds requiring that the order given by the Petitioner to the broker had to be in writing. Being in writing would simply be evidence of the fact. In this case the order was made orally. The Court below, as well as the Board of Tax Appeals, found as a true fact that such order was given to the broker. Therefore, the question as to whether it was in writing or was made orally does not enter into the picture. As was said in *Howbert v. Penrose*, 87 F. (2d) 577 (C. C. A. 10), the question as to whether it is in writing or is made orally simply goes to the proof as to what was actually done. The Court said:

> "In our opinion, proof of the certificates delivered does not conclusively determine what transaction did in fact take place. It is evidence, but not conclusive evidence. So it is of the question of intent of the seller, a point much labored at the trial and here; it is some evidence as to what was done, but not conclusive. The ultimate question is, what was done? It was, and must be, readily conceded that if there had been a written contract of the sale of this stock, specifying 'the shares purchased by me in 1916,' and a clerk in the office of a trust company had delivered certificates acquired at an earlier date, the 'identity of the lot' could be and would be determined by the contract. There being no applicable statute of frauds, the finding of the trial court, upon

ample evidence, identifies the lot as well as a written contract. * * *"

Analysis of Decisions Upon Which Circuit Court of Appeals Bases Its Decision

It must be borne in mind that this case does not involve one where there was only an *intention* to sell specific shares without anything more. We have here the uncontroverted fact that the Petitioner went further and designated the specific shares to be sold in his order to the broker.

The decisions upon which the Circuit Court of Appeals relies in the support of its decision deal with cases where there was only an intention to sell specific shares without any designation of the shares to be sold in any order or contract with the broker or third party. This is an altogether different situation than in the case at bar. An analysis of such decision discloses an intention only to sell specific shares without anything more.

In *Horner vs. Commissioner of Internal Revenue*, 72 F. (2) 407, the Petitioner was seeking to base any tax liability upon the cost of stock which he contended *that he intended to sell but which he did not yet own.* In other words, he was trying to convince the Court that the stock which he sold was stock which he did not yet own. There was no designation by instructions of any particular stock to any broker. In the case at bar, we do not have merely an intention to sell, but we do have a specific designation by instructions to the broker of the specific stock to be sold.

In *Commissioner of Internal Revenue vs. Merchants' & Manufacturers' Fire Ins. Co.*, 72 F. (2d) 408, a reading

of the decision discloses that there was no designation of the particular shares to be sold and delivered. In fact, the Court in its opinion says:

> "* * * but the particular shares to be sold and delivered would not be designated." (Page 409.)

In the case at bar we have specific designations by instructions as to the stock to be sold and not only an intention on the part of the taxpayer.

In *Horner vs. Commissioner of Internal Revenue*, 78 F. (2d) 813 (C. C. A. 3), we have again only an intention upon the part of the taxpayer to sell certain stocks, but actually delivering other certificates *without any designation to the broker as to the particular stock to be sold.* Here again is a different situation from the case at bar, where there has been in the case at bar a specific designation by instructions of the stock to be sold.

In *Vawter vs. Commissioner of Internal Revenue*, 83 F. (2d) 11, the Petitioner did not designate to the broker, or to anyone else, the particular stock which he was selling. The Petitioner kept a memorandum on an envelope, which he kept in his possession, of the stocks he intended to sell. It is, therefore, clear from a reading of the decision that if there had been a designation other than a mere intention, the decision of the Court would have been otherwise, because in the opinion the Court says:

> "The burden rested upon petitioner to show that the stock sold in 1930 was that purchased in 1929. Skinner v. Eaton (C. C. A.), 45 F. (2d) 568, certiorari denied, 238 U. S. 837, 51 S. Ct. 486, 75 L. Ed. 1449. It is argued that stock certificates are not the only means by which shares of stock may be identified; that the admitted intention of petitioner to sell

the shares acquired during the preceding year and the memoranda on the envelope were sufficient to discharge the burden. It is settled law that shares of stock can be identified otherwise than through stock certificates, but intention alone is not enough to do so. *There must be a further designation in order to establish the requisite identity.* Helvering v. Rankin, supra, Snyder v. Commissioner, supra; Miller v. Commissioner (C. C. A), 80 F. (2d) 219; Fuller v. Commissioner (C. C. A.), 81 F. (2d) 176; Skinner v. Eaton, supra. The writing on the envelope does tend to corroborate the intention, and it may be conceded that the two combined and considered apart from other facts indicate a sale of the interest in the corporation which was purchased during the previous year; but arrayed in bold contradiction is the fact that, upon receipt of the certificates representing dividends, petitioner removed certificate No. A-5720 from the envelope and placed five of the dividend certificates in it; and, in consummating the sale, he delivered the five certificates to the purchaser and retained the certificate which represented the purchase. * * *" (Emphasis ours.) (Page 13.)

It is therefore clear in the aforecited case that there was no designation of any character as to the stock to be sold, but merely a memorandum upon the taxpayer's own record as to what he intended to sell. This is entirely a different situation than the one in the case at bar, where there was a specific designation to the broker of the stock to be sold.

In *Curtis vs. Commissioner of Internal Revenue,* 89 F. (2d) 736 (C. C. A. 8), the Petitioner had purchased certain stock from the retiring manager. He had made a general agreement with a group of key employees that he would sell to them, not any specified stock, but, an amount of stock which would represent approximately one-third interest in the Company. When the retiring

manager delivered the stock to the Petitioner, the Petitioner took those shares or certificates delivered by the manager and reissued such certificates in his name and these certificates were then deposited with the retiring manager as collateral to secure the balance of the purchase price. Thereafter, the Petitioner issued from other stock which he held the certificates representing the sale to the employees. The petitioner contended before the Court that the certificates of stock or the stock sold to the employees was that purchased from the retiring manager. The answer was, of course, obvious, because the Court said:

> "* * * It falls short of showing that either petitioner or any of the employees had in mind that the stock sold and bought must or should be that represented by the exact certificates held by Schellberg and his wife. No one of the employees so testifies. Petitioner's own actions are proof that the identity of the shares was not material to him since, with complete control of the matter, he deposited these precise shares as collateral and later made the transfer to the employees from other shares." (Page 738.)

There was, therefore, no designation of any particular stock which he would sell to the employees, and there was no contract of the particular stock which they were to purchase. He actually delivered stock from another lot which he had in his possession and had placed the stock which he says he intended to sell as collateral with the purchaser from whom he bought it.

This is an entirely different situation from the facts presented in the case at bar, where there is a specific designation and order for the specific stock to be sold.

In *Cole vs. Helburn*, 4 F. Supp. 20, there was no designation or direction to the broker to sell any specific

stock. If there had been, the decision of the Court would have been different, because the Court says:

> "I cannot sustain plaintiff's contention with reference to the sale of the Atlantic Coast Line Railroad Company stock. He did not direct his broker to sell any particular stock. He simply directed him to sell three hundred shares, and, when the time came for plaintiff to deliver the property sold, he delivered certificates representing the stock purchased by him on February 24, 1928. There is no claim that plaintiff and the purchaser of this stock had any agreement or understanding as to the particular shares of stock involved in the transaction. Therefore, there can be no contention successfully made that the minds of the parties were in agreement, as to the particular shares of stock bought, and that by mistake other and different shares were delivered. The only mistake was made by the plaintiff himself, and for this he must suffer. * * *" (Page 232.)

Here again is a decision where the Petitioner did not designate the specific stock to be sold. There was no agreement or understanding as to the stock to be involved in the transaction. The Court in its decision recognizes that if there had been such a designation of a particular lot of stock, such designation would have been recognized. How different from the situation in the case at bar, where the Petitioner specifically designates the stock to be sold by instructions to the broker and as to which particular lot of stock there can be no question as to identity.

In *Skinner vs. Eaton*, 45 F. (2d) 568, the contention of the taxpayer was based upon statements made by the decedent that he intended to retain his original holdings and that he intended to sell certain stock purchased for return. Again no designation or contract with reference to any specific stock. The Court in its opinion says:

> "In support of their claim, the appellant argue that the sales of 287 shares for 1917 were of stock purchased before March 1, 1913, and 150 shares for 1919 were stock purchased after March 1, 1913, and rely upon the testimony of the associates of the taxpayer, who said that the decedent told them he intended to retain his original holdings in the corporation, and that he intended to sell certain stock purchased for return. These statements are alleged to have been made in 1914 and 1915. The declarations of a taxpayer as to his intention to sell the more recently purchased stock and to retain his original holdings, made orally, are insufficient to change the result. They indicate merely a purpose which he may not have adhered to. They in no way marked the particular shares of stock here under consideration, the identity of which the trial judge has found to have been lost." (Page 570.)

Here again the facts and circumstances were different than in the case at bar. In the cited case, there was merely an expressed intention, while in the case at bar there is a specific and expressed designation by instructions of the stock to be sold.

In *Snyder vs. Commissioner of Internal Revenue*, 295 U. S. 134, we again have a case where there was no designation of the particular stock to be sold, because the Court in its opinion says:

> "* * * The only attempt at identification found by the Board, was the uncontradicted testimony of Snyder to the effect that 'in each case where a sale was made it was his intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount in order to increase his margin and acquire additional shares of the stock.' " (Page 137.)

In *Remington Rand vs. Commissioner of Internal Revenue*, 33 F. (2d) 77, the facts and the issue involved

do not in any manner bear any relation to the facts and issue involved in the case at bar. The quotation therefrom that tax liabilities must be determined by what in fact was done does not detract in any manner from the decisions cited by the Petitioner, wherein the Courts have recognized that the designation of a specific stock to be sold to the broker is sufficient evidence of what was done to base any tax liability upon the sale of the stock so designated.

CONCLUSION

We therefore respectfully contend that the proper yardstick in determining the situation is that laid down by Judge Hand in *Miller vs. Commissioner of Internal Revenue,* 80 F. (2d) 219, where at page 221 the Court says:

> "It follows from the foregoing: (1) That where there is no designation by the taxpayer at the time of making the sale the certificate should be treated as the proper means for identification; (2) that a designation by instructions to the broker of the shares to be sold is controlling though the certificate delivered does not correspond with the instructions; (3) that the 'First-in, First-out' rule applies only where there is neither identification by a certificate, nor by designation of the taxpayer."

We respectfully contend that the situation of the Petitioner in the case at bar falls within subdivision (2) of the rule of law above cited in the opinion of Judge Hand. The Petitioner had made a specific and clear designation by instructions to the broker as to the stock the Petitioner ordered sold. Through mistake in delivery, the bank clerk delivered certificates of other stock. Under the rules of law and decisions cited by the respondent,

this did not change the force and effect of the designation which the Petitioner had made to the broker as to the stock which he was selling in that transaction.

We therefore respectfully contend that the Petitioner's contentions should be sustained and that the decision of the Circuit Court of Appeals should be reversed.

Respectfully submitted,

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61867—38

In the Supreme Court of the United States

OCTOBER TERM, 1937

No. 912

JAMES E. DAVIDSON, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 10–22) is reported at 34 B. T. A. 555. The opinion of the Circuit Court of Appeals (R. 35–40) is reported at 94 F. (2d) 300.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on January 31, 1938 (R. 40–41). A petition for rehearing was denied February 22, 1938 (R. 42). The petition for writ of certiorari was filed April 1, 1938. The jurisdiction of this

Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the taxable gain from the sale of 1,000 shares of certain stock is to be determined, as the Board and the court below held, upon the basis of the cost of the shares which the taxpayer actually sold, as represented by the certificates actually delivered to the broker by a bank (through a mistake of the bank), which certificates have been identified, rather than, as the taxpayer claims, upon the basis of the cost of the shares which he intended to sell and instructed the bank to deliver and the broker to sell.

STATUTE INVOLVED

Revenue Act of 1928, c. 852, 45 Stat. 791:

> SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.
>
> (a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.
>
> * * * * *
>
> SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.
>
> (a) *Property acquired after February 28, 1913.*—The basis for determining the gain or

loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; * * *

* * * * *

STATEMENT

The facts relevant to the question here presented, as found by the Board,[1] may be stated as follows (R. 14):

On March 27, 1929, the taxpayer, through his broker, purchased 1,000 shares of National Power & Light Company stock with a part of the proceeds of a loan from the Omaha National Bank, certificates for which, numbered 80,250 to 80,258, inclusive, and 80,264, were delivered to the taxpayer and were put up as collateral with the bank (R. 14).

On June 19, 1929, the taxpayer instructed his broker to sell 500 of the 1,000 shares purchased on March 27, 1929, the certificates for which were on deposit at the bank. When the sale was made the taxpayer called at the bank to get the certificates for delivery to the broker, but the bank refused to release them to the taxpayer, stating that it would make delivery itself. The taxpayer then instructed the bank to deliver 500 shares from the certificates numbered 80,250 to 80,258, inclusive,

[1] The opinion of the Board (R. 10–22) covering both this case and a companion case in which the taxpayer's wife is the taxpayer and the petitioner in *Edith L. Davidson* v. *Commissioner*, No. 913 in this Court, contains the relevant facts under that portion of the Board's findings of fact headed "National Power & Light Co. transactions of James E. Davidson in 1929" (R. 13–14).

and 80,264. In making delivery, however, a bank clerk, by mistake, delivered certificates from another lot which had been held as collateral by the bank since 1925. The mistake was not known to the taxpayer at that time (R. 14).

On July 1, 1929, the taxpayer instructed the broker to sell the remaining 500 shares purchased on March 27, 1929, and instructed the bank to deliver to the broker the remaining 500 shares from the certificates above mentioned. Again, however, the bank made the same mistake and delivered to the broker certificates for 500 shares from the lot which had been held as collateral since 1925 (R. 14).

The aggregate proceeds from the sale of these 1,000 shares were $59,435. The cost of the 1,000 shares purchased on March 27, 1929, was $49,900. The cost of the 1,000 shares which were delivered to the broker by mistake was $4,420 (R. 14).

In his return, and in his appeals to the Board (R. 3–5) and to the court below (R. 25–29), the taxpayer claimed that his gain should be computed upon the basis of the cost of the 1,000 shares which he intended to sell. The Board of Tax Appeals held (R. 18–20) that the shares delivered to the broker were the shares actually sold by the taxpayer, and that the taxable gain is to be determined upon the basis of the cost of the shares represented by the certificates which were actually delivered to the broker. The court below affirmed the decision of the Board (R. 35–40).

DISCUSSION

The court below recognized that its decision is in conflict with "the broad holding" of the Circuit Court of Appeals for the Second Circuit in *Miller* v. *Commissioner,* 80 F. (2d) 219. The conflict is the result of differing interpretations of this Court's opinion in *Helvering* v. *Rankin,* 295 U. S. 123. We believe that the decision of the court below is correct and that the court in the *Miller* case misconceived the meaning of this Court's decision in *Helvering* v. *Rankin, supra.* While the *Miller* case is perhaps distinguishable from the present case, on the ground hereafter stated, we do not, in view of the undoubted inconsistency in the interpretations of this Court's opinion in the *Rankin* case, oppose the grant of a writ of certiorari herein.

In the present case, although the taxpayer's intention was to sell the 1,000 shares acquired on March 27, 1929, at a cost of $49,900, and although he so instructed his broker and later instructed the bank to deliver to the broker those specific shares, what actually took place was that in consummation of the sale 1,000 other shares, which have been identified as shares bought on a prior date at a cost of $4,420, were delivered to the broker and were sold. Controversy, therefore, centers upon the effect to be given to the taxpayer's intention, where that intention was not carried out in consummating the sale. Admittedly, the failure to carry out that intention was due to a mistake of the bank, or

of the bank clerk. But other shares were, in fact, actually sold, as represented by the certificates delivered by the bank, which, as suggested in both opinions below (R. 20, 39), must be regarded as the taxpayer's agent (at least for the purposes of the present controversy). Under the circumstances, the court below correctly held that the tax liability must be determined by what in fact was done. *United States* v. *Phellis*, 257 U. S. 156, 172; *United States* v. *Safety Car Heating Co.*, 297 U. S. 88, 98; *Bonham* v. *Commissioner*, 89 F. (2d) 725, 728 (C. C. A. 8th); *Curtis* v. *Commissioner*, 89 F. (2d) 736, 738 (C. C. A. 8th); *Remington Rand, Inc.*, v. *Commissioner*, 33 F. (2d) 77, 78 (C. C. A. 2d).

The decision below is in keeping with the principles laid down in *Curtis* v. *Commissioner*, *supra*; *Vawter* v. *Commissioner*, 83 F. (2d) 11 (C. C. A. 10th), certiorari denied, 299 U. S. 578; *Horner* v. *Commissioner*, 72 F. (2d) 407 (C. C. A. 3d); *Commissioner* v. *Merchants' & Mfrs.' F. Ins. Co.*, 72 F. (2d) 408 (C. C. A. 3d); *Cole* v. *Helburn*, 4 F. Supp. 230 (W. D. Ky.); *Skinner* v. *Eaton*, 45 F. (2d) 568 (C. C. A. 2d), certiorari denied, 283 U. S. 837; *Horner* v. *Commissioner*, 78 F. (2d) 813 (C. C. A. 3d).

We think that the court below was clearly correct in holding that a decision in favor of the taxpayer was not required by this Court's decision in *Helvering* v. *Rankin*, *supra*. In that case the tax-

payer had been trading in stocks on a marginal account and identification by certificates was impossible. The case holds only that identification by certificate is not the only means of identification, and that, where that is impossible, the taxpayer may resort to identification by dates or cost of purchases in a communication or selling instruction to the broker so as to avoid the application of the so-called "first in, first out" rule. Of course, there is no question of the application of that rule here, because the shares sold have been definitely identified. For the same reason, as the court below properly recognized, there is no occasion for resort to selling instructions.

In *Miller* v. *Commissioner, supra,* where stock was in the possession of the broker, the taxpayer in a communication to the broker directed him to sell certain shares purchased on certain dates, but in consummating the sale the broker delivered certificates representing other shares. The court there came to the conclusion (p. 221):

> * * * that a designation by instructions to the broker of the shares to be sold is controlling though the certificate delivered does not correspond with the instructions; * * *

This holding, we think, represents a misconception of the *Rankin* case. That case, far from holding that a designation by instructions to the broker is controlling, recognized that identification by certificate is the ordinary, and the best, means of

identification, and that other means are permissible only where identification by certificate is not possible.

While the broad holding of the *Miller* case as quoted above is thus in conflict with the holding below, it should be pointed out that upon the particular facts of the two cases a distinction exists. In the *Miller* case, the shares were already in the possession of the broker when the instructions to sell were given, whereas in the present case they were in the possession of the taxpayer's agent, the bank, and so remained subject to the taxpayer's control. This distinction, which the court below recognized (R. 39), and which the Board held to be controlling (R. 19), is suggested even by the *Miller* case, where the court, in speaking of some of the cases hereinabove referred to, said (p. 221):

> But in each of these cases the taxpayer himself had custody of the certificates * * *.

The same distinction applies to *Millikan* v. *Commissioner*, 83 F. (2d) 213 (C. C. A. 2d), cited in the petition, where the certificates were likewise in the possession of the broker.

The petitioner's assertion of conflict with other decisions of the circuit courts of appeals (Pet. 4–5) is without merit. *Fuller* v. *Commissioner*, 81 F. (2d) 176 (C. C. A. 1st), and *Kraus* v. *Commissioner*, 88 F. (2d) 616 (C. C. A. 2d), are distinguishable in that they involved situations where identification by certificates was impossible be-

cause the shares held by the taxpayer had been exchanged for new shares in a nontaxable exchange. *Howbert* v. *Pennrose*, 38 F. (2d) 577 (C. C. A. 10th), is distinguishable from the instant case because there it was found *as a fact* that the shares the taxpayer intended to sell were actually sold, as the appellate court pointed out (p. 578):

> The trial court found as a fact from the evidence, that "plaintiff intended to *and did sell*" the shares acquired in 1916 and 1917. [Italics supplied.]

CONCLUSION

While we believe that the court below correctly applied the statute to the facts of this case, we do not oppose the grant of certiorari in view of the conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Miller* v. *Commissioner, supra.*

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APRIL 1938.

U. S. GOVERNMENT PRINTING OFFICE: 1938

In the Supreme Court of the United States

OCTOBER TERM, 1938

JAMES M. LANDIS, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

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100442—38——1

In the Supreme Court of the United States

OCTOBER TERM, 1938

No. 18

JAMES E. DAVIDSON, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 9–22) is reported at 34 B. T. A. 555. The opinion of the Circuit Court of Appeals (R. 32–37) is reported at 94 F. (2d) 300.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on January 31, 1938 (R. 38). A petition for rehearing was denied February 22, 1938 (R. 39). The petition for a writ of certiorari was

filed April 1, 1938, and was granted May 16, 1938 (R. 43). The jurisdiction of this Court is conferred by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the taxable gain from the sale of 1,000 shares of certain stock is to be determined, as the Board and the court below held, upon the basis of the cost of the shares which the taxpayer actually sold as represented by the certificates actually delivered to the broker by a bank (through a mistake of the bank), which certificates have been identified, rather than, as the taxpayer claims, upon the basis of the cost of the shares which he intended to sell and which he instructed the broker to sell and the bank to deliver to the broker.

STATUTE INVOLVED

Revenue Act of 1928, c. 852, 45 Stat. 791:

> SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.
>
> (a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.
>
> * * * * *

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; * * *

* * * * * *

STATEMENT

The facts relevant to the question here presented, as found by the Board,[1] may be stated as follows (R. 13–14):

On March 27, 1929, the taxpayer, through his broker, purchased 1,000 shares of National Power & Light Company stock with a part of the proceeds of a loan from the Omaha National Bank. Certificates for these shares of stock numbered 80250 to 80258, inclusive, and 80264, were delivered to the taxpayer and were put up as collateral with the bank (R. 13).

On June 19, 1929, the taxpayer instructed his broker to sell 500 of the 1,000 shares purchased on March 27, 1929, the certificates for which were on

[1] The findings of fact and opinion of the Board (R. 9–22) covering both this case and a companion case in which the petitioner's wife was the taxpayer (and in which this Court denied the petition for a writ of certiorari on May 16, 1938, *Edith L. Davidson* v. *Commissioner*, No. 913, October Term, 1937) contains the relevant facts under that portion of the Board's finding of fact headed "National Power & Light Co. Transactions of James E. Davidson in 1929" (R. 12–14).

deposit at the bank. When the sale was made the taxpayer called at the bank to get the certificates for delivery to the broker, but the bank refused to release them to the taxpayer, stating that it would make delivery itself. The taxpayer then instructed the bank to deliver 500 shares from the certificates numbered 80,250 to 80,258, inclusive, and 80,264. In making delivery, however, a bank clerk, by mistake, delivered certificates from another lot which had been held as collateral by the bank since 1925. The mistake was not known to the taxpayer at that time (R. 13-14).

On July 1, 1929, the taxpayer instructed the broker to sell the remaining 500 shares purchased on March 27, 1929, and instructed the bank to deliver to the broker the remaining 500 shares from the certificates above mentioned. Again, however, the bank made the same mistake and delivered to the broker certificates for 500 shares from the lot which had been held as collateral since 1925 (R. 14).

The aggregate proceeds from the sale of these 1,000 shares were $59,435. The cost of the 1,000 shares purchased on March 27, 1929, was $49,900. The cost of the 1,000 shares which were delivered to the broker by mistake was $4,420 (R. 14).

In his return, and in his appeals to the Board (R. 2-5) and to the court below (R. 25-29), the taxpayer claimed that his gain should be computed upon the basis of the cost of the 1,000 shares which

he intended to sell. The Board of Tax Appeals held (R. 18-20) that the shares delivered to the broker were the shares actually sold by the taxpayer, and that the taxable gain is to be determined upon the basis of the cost of the shares represented by the certificates which were actually delivered to the broker. The court below affirmed the decision of the Board (R. 32-37).

SUMMARY OF ARGUMENT

The statute requires that the gain be determined on the cost basis of the shares actually sold and not upon the different basis of other shares of the same stock which the taxpayer intended to sell and instructed his broker to sell. The taxpayer actually sold the shares identified by the certificates delivered in consummation of the sale and not the shares represented by the certificates which he requested the bank to deliver. The taxpayer's designation of the shares he intended to sell in his instructions to the broker does not prevail over the ordinary means of identification of the shares sold by the certificates delivered on the sale. The tax liability was correctly determined upon what was actually done and not upon what was intended to be done.

ARGUMENT

THE TAXABLE GAIN HAS BEEN COMPUTED CORRECTLY UPON THE BASIS OF THE COST OF THE SHARES ACTUALLY SOLD, AS REPRESENTED BY THE CERTIFICATES DELIVERED

On March 27, 1929, the taxpayer through his broker purchased shares of stock with part of the proceeds of a loan from a bank. Certificates for these shares were delivered to the taxpayer and put up as collateral with the bank (R. 13). Later in the same year the taxpayer instructed his broker to sell these shares purchased on March 27, 1929, and instructed the bank to deliver upon the sale the identical certificates which the taxpayer had received when he purchased these shares. By mistake the bank delivered certificates for other shares of the same stock which had been held by the bank as collateral since 1925 and which had a lesser basis for computation of gain. The taxpayer did not know about the mistake at that time (R. 14).

The taxpayer contends, on these undisputed facts, that the instructions to the broker identified the shares sold for purposes of the tax even though the certificates delivered upon the sale in fact represented other shares purchased at a different time. The respondent contends (A) that the statute requires the gain to be determined upon the cost of the shares actually sold and (B) that the certificates delivered upon the sale identified the shares actually sold, prevailing over the instruc-

tions to the broker as the means of identification of the shares sold.

A. GAIN MUST BE COMPUTED ON THE SHARES ACTUALLY SOLD

Section 111 of the Revenue Act of 1928 provides that the "gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, * * *." Section 113 (a) provides that the "basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; * * *"

The respondent contends that this statute requires that the gain be determined on the cost of property sold including shares of stocks if they can be identified, and does not permit that gain to be determined on the different cost basis of similar property or shares which the taxpayer intended to sell but by mistake, of himself or of others, failed to sell.

The taxpayer has the right to have the tax determined on the shares he chooses to sell and does sell rather than other shares which he might have sold (*Helvering* v. *Rankin*, 295 U. S. 123, 129–130) and, conversely, he is bound to pay the tax computed on the shares actually sold.

The court below correctly observed (R. 37) that tax liability must be determined by what in fact is done. *United States* v. *Safety Car Heating Co.*, 297 U. S. 88, 98; *United States* v. *Phellis*, 257 U. S.

156, 172. This rule is applied to this situation in which a taxpayer intends to sell certain shares of stock but in fact sells other shares, as represented by the certificates delivered. The tax is computed on the cost of the shares actually sold, whether or not the intention to sell other shares is expressed at the time of the sale. *Curtis* v. *Commissioner*, 89 F. (2d) 736, 738 (C. C. A. 8th); *Vawter* v. *Commissioner*, 83 F. (2d) 11, 13 (C. C. A. 10th), certiorari denied, 299 U. S. 578; *Horner* v. *Commissioner*, 78 F. (2d) 813, 814 (C. C. A. 3d); *Commissioner* v. *Merchants' & Mfrs. F. Ins. Co.*, 72 F. (2d) 408 (C. C. A. 3d); *Horner* v. *Commissioner*, 72 F. (2d) 407, 408 (C. C. A. 3d). The question in each case is which shares actually were sold.

B. THE CERTIFICATES DELIVERED, RATHER THAN THE INSTRUCTIONS TO THE BROKER, IDENTIFIED THE SHARES SOLD

The difference between the sale of stock and other personal property is that it is often difficult, and sometimes impossible, as a matter of proof, to identify the particular shares sold. In this case, however, the undisputed facts are that particular certificates identify particular shares according to the time of purchase. Ten separately numbered certificates were delivered to the taxpayer for the 1,000 shares of stock purchased on March 27, 1929. These identical certificates were deposited as collateral with the bank, which also held other certificates for 2,200 shares of the same stock deposited as collateral in 1925 (R. 11, 14). The bank continued to hold these identical certificates which

continued to represent, identify, and distinguish the shares purchased in 1925 and 1929.

Indeed, the taxpayer in his transactions with these shares of this stock always carefully recognized and never ignored the fact that particular certificates represented particular shares of stock according to the time of purchase. His conduct discloses that he considered that the certificates which he directed the bank to deliver upon the sales in question represented shares purchased on March 27, 1929, and that certificates delivered by mistake represented the shares acquired in 1925.

1. The taxpayer's contention (Br. 27–29) that he did sell the shares purchased in 1929, despite the consummation of the sale by the delivery of the certificates which identified, and which the taxpayer always treated as identifying, the shares purchased in 1925 is not supported, as the taxpayer claims, by *Richardson* v. *Shaw*, 209 U. S. 365, and *Gorman* v. *Littlefield*, 229 U. S. 19, or by *Duel* v. *Hollins*, 241 U. S. 523. Those cases held that upon a broker's bankruptcy, his customers, without identifying the particular certificates of stock deposited with or held by the broker for their accounts, could recover from the bankrupt estate, as their own property without an unlawful preference, different certificates as representing their shares of the stock.

Those decisions have no application here. They are based upon the relation of broker and customer under which "the broker has an implied authority to substitute other securities of the same kind and

amount for the securities which he holds for his customer, * * *." *Provost* v. *United States*, 269 U. S. 443, 455. Under this implied authority the substituted securities become the customer's property and the broker's disposition of the certificates deposited by the customer is not a conversion of the customer's property. It was in connection with this element in the relation of broker and customer under which substituted certificates represent a customer's shares, that the Court stated that identification of particular certificates was unimportant and that substitution of certificates did not change the property right held by the broker for the customer. *Gorman* v. *Littlefield*, 229 U. S. 19, 25; *Richardson* v. *Shaw*, 209 U. S. 365, 378-379.

Moreover, those cases were concerned only with the question of substituted certificates representing all the shares of a customer without distinguishing between different shares owned by the same customer and have no application here where the problem is one of identification between two lots of shares of the same shareholder. Indeed, even the taxpayer must claim that lots of stock can be distinguished in some manner in order to claim that a certain lot was sold and to avoid the first-in first-out rule which is provided by Treasury regulations and applies when the shares sold cannot be identified. For purposes of recovery of shares pledged with a broker they may be treated as

fungible, but for the present purpose where identification of the shares sold is all important they should be treated as distinct articles of personal property. So considered, it is clear on the undisputed facts that the shares purchased in 1925, and not the shares purchased in 1929, were sold.

2. The taxpayer contends (Br. 21) that his instructions to the broker to sell the shares purchased in 1929 control even though the bank upon the sale delivered certificates which identified the shares purchased in 1925. The respondent submits that such instructions may be recognized as a means of identifying the stock sold only in unusual circumstances not present here, when the ordinary means of identification, the certificates, is not available, such as where a taxpayer is trading on margin and his shares are not represented by particular certificates and identification by certificates is impossible. In such a situation the taxpayer might have been left, because of inability to have his stock identified by particular certificates, to accept the first-in first-out rule. Another alternative, however, has been adopted by this Court and, in addition to the ordinary means of identification by certificate, taxpayers in some situations have been allowed to identify shares sold by instructions to a broker to sell shares purchased at a particular time. *Helvering* v. *Rankin*, 295 U. S. 123.

Where, as here, identification by certificate is possible it controls and the shares sold are determined by the certificates delivered upon the sale. The decision of the court below to this effect is supported by the similar rulings in other cases. *Curtis* v. *Commissioner*, 89 F. (2d) 736, 738; *Vawter* v. *Commissioner*, 83 F. (2d) 11 (C. C. A. 10th), certiorari denied, 299 U. S. 578; *Horner* v. *Commissioner*, 78 F. (2d) 813 (C. C. A. 3d); *Skinner* v. *Eaton*, 45 F. (2d) 568 (C. C. A. 2d), certiorari denied, 283 U. S. 837.

While we believed the decision of the court below to be correct, we did not oppose a granting of the writ of certiorari herein for the reason that the court below had recognized (R. 36) that its decision was not consistent with the "broad holding" of *Miller* v. *Commissioner*, 80 F. (2d) 219 (C. C. A. 2d), as to the meaning of this Court's opinion in *Helvering* v. *Rankin*, 295 U. S. 123—and, further, we did not oppose it, although we felt that the *Miller* case might be distinguished from the present case, on the ground hereinafter stated.

In *Helvering* v. *Rankin*, *supra*, this Court held that where the taxpayer has been trading in stocks on a marginal account and identification by certificates is impossible, certificate identification is not the only means of identification, and the taxpayer may resort to identification by dates or cost of purchases in a communication or selling instruction to the broker so as to avoid the application of the first-in first-out rule. There is no question

here of the application of that rule which is applicable only where stock which can not be identified is sold from stock which had been acquired on various dates and at various prices. Here, the stock sold by the taxpayer has been identified.

In *Miller* v. *Commissioner, supra,* the taxpayer directed the broker to sell certain shares purchased on certain dates and then in the broker's possession, but in consummating the sale the broker delivered certificates representing other shares. The court there concluded (p. 221):

> * * * that a designation by instructions to the broker of the shares to be sold is controlling though the certificate delivered does not correspond with the instructions; * * *

This holding that instructions to the broker should prevail over identification by certificates represents, we think, a misconception of the *Rankin* case We submit that the *Rankin* case means only that in the absence of certificate identification, identification by designation of dates or cost of purchases to the broker will suffice, or, stated differently, that in the absence of a better (certificate) identification, the designation by dates of purchase will be sufficient. This Court's opinion in the *Rankin* case means, we submit, as the court below thought (R. 36), that certificate identification is the ordinary and the best means of identification of shares sold, but where, such as by reason of the nature of the dealings in a marginal account,

identification by certificates is not possible, then, identification by designation of dates in a communication to the broker will suffice.

But, even if the *Miller* case correctly interprets the *Rankin* decision, the decision below can be sustained upon a distinction existing in the facts. In the *Miller* case the shares were already in the possession of the broker when the instructions to sell were given, and thus nothing further remained to be done by the seller, whereas in the present case the shares were in the possession of the taxpayer's agent, the bank, so that they were in the possession of the taxpayer as between him and the broker, and the sale was to be consummated by their delivery to the broker—and so they remained subject to the taxpayer's control. This distinction, which the court below recognized (R. 36–37) and which the Board held to be controlling (R. 19), is suggested even by the *Miller* case, where the court, in speaking of some of the cases hereinbefore referred to, said (p. 221):

> But in each of these cases the taxpayer himself had custody of the certificates * * *.

The same distinction applies to *Milliken* v. *Commissioner*, 83 F. (2d) 213 (C. C. A. 2d), where the certificates were likewise in the possession of the broker.

3. After the decision in the *Miller* case, the question of whether taxable gain should be determined upon the basis of the cost of the shares which were actually sold, as represented by the certificates de-

livered, rather than upon the basis of the cost of the shares which the taxpayer intended to sell, was considered in *Vawter* v. *Commissioner, supra,* and *Curtis* v. *Commissioner, supra.* In the *Vawter* case the intention to sell certain specified shares was admitted, and that intention was corroborated by certain entries made by the taxpayer on his records, but certificates representing other shares were delivered by the taxpayer in consummation of the sale. In the *Curtis* case the taxpayer claimed that he intended to sell certain shares which he had acquired on a certain date, but in consummating the sale he delivered certificates representing other shares, and retained those which he intended to sell, or, rather, allowed those which he intended to sell to remain in the possession of a third party as collateral. In both cases the holding of the *Miller* case was relied upon in urging that the taxpayer's intention to sell certain specified shares should prevail over the certificates as the means of identification of the shares sold. Both cases held that gains should be determined upon the basis of the shares represented by the certificates delivered in consummating the sale.

While both of those decisions thus are in keeping with the decision below, they did not involve the precise question presented here, because they did not involve any communication to the broker. They are also distinguishable from the present case in the fact that here the delivery of other certificates in the consummation of the sale came about

by reason of the mistake of the bank. In this respect they are like the companion case of *Edith L. Davidson* v. *Commissioner*, 94 F. (2d) 303 (C. C. A. 8th), certiorari denied May 16, 1938, where the substitution of other certificates in consummating the sale came about solely because of the taxpayer's own act—and not because of the failure of the broker (as in the *Miller* case) or the mistake of the bank (as here). But we submit that in the final analysis this distinction should have no controlling effect because the bank was the custodian of the shares for the taxpayer and should (at least for the purposes of the present controversy) be regarded as the agent of the taxpayer, as suggested in both opinions below (R. 20, 37). The result should be no different than if a private secretary or other employee of the taxpayer had been holding the shares for the taxpayer and had, upon being instructed to make the delivery, delivered the wrong certificates. Clearly, the mistake of the secretary would be regarded as the taxpayer's own mistake, and we submit the mistake of the bank must be treated, for the purposes of the present controversy, as the mistake of the taxpayer.

None of the other cases passes upon the precise question presented. *Snyder* v. *Commissioner*, 295 U. S. 134, dealt, like the *Rankin* case, with a situation where identification by certificates was impossible. *Fuller* v. *Commissioner*, 81 F. (2d) 176 (C. C. A. 1st), and *Kraus* v. *Commissioner*, 88 F. (2d) 616 (C. C. A. 2d), also presented a situation

where identification by certificate was impossible, because the shares held by the taxpayer had been exchanged for new shares of stock in a non-taxable exchange. *Howbert* v. *Penrose,* 38 F. (2d) 577 (C. C. A. 10th), is distinguishable from the instant case because there it was found *as a fact* that the shares the taxpayer intended to sell were actually sold, as the appellate court pointed out (p. 578):

> The trial court found as a fact from the evidence, that "plaintiff intended to *and did sell*" the shares acquired in 1916 and 1917. [Italics supplied.]

4. It is submitted, in conclusion, that the decision of the court below is not only logical but also practical. Where certificate identification is possible, it should be controlling as the means of identification. On the other hand, the adoption of the rule contended for by the taxpayer would result in confusion, for when the taxpayer comes to sell certificates representing the shares bought on March 27, 1929 (which he intended to sell but did not sell in the transaction here involved), the problem then arises as to which shares he will then be selling. Moreover, to adopt the contention of the taxpayer would open the door to fraud, as the court below recognized (R. 37), by making possible collusion between the broker and the taxpayer—a result to be, if reasonably possible, avoided in taxation. And finally, it may be added that, of course, no arbitrary deprivation of the right of the seller to select the shares he desires to sell (*Rankin* opinion,

p. 129–130) results from a rule which merely requires the taxpayer to identify by the best possible means the shares he sells.

CONCLUSION

The decision below is correct and should be affirmed.

Respectfully submitted.

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OCTOBER 1938.

U. S. GOVERNMENT PRINTING OFFICE: 1938

SUPREME COURT OF THE UNITED STATES.

No. 18.—October Term, 1938.

James E. Davidson, Petitioner,
vs.
Commissioner of Internal Revenue.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Eighth Circuit.

[November 7, 1938.]

Mr. Justice Butler delivered the opinion of the Court.

Upon petitioner's insistence and respondent's admission, that the decision below conflicts with that of the circuit court of appeals for the second circuit in *Miller* v. *Commissioner*, 80 F. (2d) 219, we granted a writ of certiorari. — U. S. —. The question presented is whether petitioner's taxable gain from sale in 1929 of 1,000 shares of stock is to be determined upon the basis of the cost of stock petitioner bought in that year, or upon the basis of lower cost of like shares earlier bought by him.

The details found by the board of tax appeals may be given briefly. March 27, 1929 at cost of $49.90 each, petitioner bought 1,000 shares for which he received 10 separately numbered certificates covering 100 shares each and delivered them to a bank to be held as security for a loan. Some years earlier he had bought, at cost of $4.42 each, 1,000 shares of like stock for which he obtained certificates that he delivered to the same bank as collateral security, where they were held until the sales here involved. June 19, 1929 petitioner instructed his broker to sell 500 shares of the stock he bought March 27, and, to enable the broker to deliver, petitioner instructed the bank to give the broker certificates covering shares bought in that year. By mistake the bank delivered him certificates of shares included in the lot earlier purchased by petitioner. July 1, 1929 petitioner instructed the broker to sell the rest of the lot bought in that year and directed the bank to deliver the broker certificates of the stock petitioner intended to have sold. Again failing to follow instructions, the bank delivered the broker certificates of stock in the other lot. It may be taken as granted that,

when he made his return, petitioner excusably assumed that the bank had followed his directions.

He reported gain on the basis of cost of the stock purchased in that year. The commissioner calculated gain on the basis of cost of the stock earlier purchased and gave notice of deficiency. The board of tax appeals sustained his determination. 35 B. T. A. 555. The circuit court of appeals affirmed. 94 F. (2d) 300.

Petitioner contends that by his reference to amounts and dates of purchases, he adequately designated to the broker the shares to be sold; that in fact the shares so identified were sold and that the bank's delivery of certificates of other stock to the broker did not affect petitioner's order. Undoubtedly, petitioner sufficiently indicated to the broker and to the bank the shares he intended to sell. He plainly allocated the lots to be sold to the 1,000 shares he bought in 1929. But it does not follow that they were the shares sold. His intention to sell, even when coupled with his order to the broker and direction to the bank, cannot be held to constitute sale. *Snyder* v. *Commissioner*, 295 U. S. 134, 137. Notwithstanding his order to the broker to sell shares in the 1929 lot, petitioner was free later to direct that shares from the other lot be used for final consummation of the sale. And so, when the bank delivered him certificates of stock not designated in his order to sell, the broker may well have assumed that petitioner's final purpose was to sell the shares covered by the certificates that the bank sent him. He had no reason to suppose that the bank did not act in accordance with instructions given it by petitioner. The case is not different from what it would have been, if petitioner himself had delivered to the broker the certificates sent by the bank. Plainly, petitioner's contention that the certificates used to complete the sale did not cover the shares sold cannot be upheld. *Commissioner* v. *Rankin*, 295 U. S. 123, 128. The commissioner rightly computed gain on the basis of what was done rather than on what petitioner intended to do. *United States* v. *Phellis*, 257 U. S. 156, 172; *Bonham* v. *Commissioner*, 89 F. (2d) 725, 728; *Curtis* v. *Commissioner*, 89 F. (2d) 736, 738; *Remington Rand, Inc.* v. *Commissioner*, 33 F. (2d) 77, 78.

Affirmed.